No. 80-1684

Office-Supreme Court, U.S.
FILED
APR 7 1981
ALEXANDER L. STEVAS,
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

PEAT, MARWICK, MITCHELL & Co.,
ANTHONY M. NATELLI and JOSEPH SCANSAROLI,

Petitioners,

v.

WACHOVIA BANK AND TRUST Co., N.A., MELLON BANK, N.A., FIRST WISCONSIN TRUST Co., THE DREYFUS OFFSHORE TRUST, N.V., and NATIONAL FIRE INSURANCE Co. OF HARTFORD,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

WILLIAM E. HEGARTY
80 Pine Street
New York, New York 10005
(212) 825-0100

Counsel of Record

VICTOR M. EARLE, III
345 Park Avenue
New York, New York 10022

Attorneys for Petitioners

Of Counsel:

MATHIAS E. MONE
JOSEPH W. MUCCIA
CAHILL GORDON & REINDEL
80 Pine Street
New York, New York 10005

April 1981

Questions Presented

1. May a federal court create a damage remedy under § 17(a) of the Securities Act of 1933 or § 10(b) of the Securities Exchange Act of 1934 for purchasers of securities who cannot establish the elements of any of the express causes of action which those Acts provide injured securities purchasers?

2. May a litigant avoid the retroactive effect of a previous decision when he is unable to show that all three factors of *Chevron Oil Co.* v. *Huson*, 404 U.S. 97 (1971), favor prospective-only effect?

Parties Below

Plaintiffs-appellants-cross appellees in the court of appeals were Wachovia Bank and Trust Co., N.A., Mellon Bank, N.A., First Wisconsin Trust Co., The Dreyfus Offshore Trust, N.V., and National Fire Insurance Co. of Hartford. The defendants-appellees-cross-appellants were Cortes W. Randell, James F. Joy, Roger O. Walther, Peat, Marwick, Mitchell & Co., Anthony M. Natelli, Joseph Scansaroli, Donald A. Fergusson, Robert A. Fergusson, White & Case and Marion J. Epley, III. The defendants-appellees were John G. Davies, Bernard J. Kurek and Dennis M. Kelly.

TABLE OF CONTENTS

PAGE

Questions Presented i

Parties Below i

Table of Contents ii

Table of Authorities iii

Opinions Below 1

Jurisdiction 1

Statutory Provisions 2

Statement of the Case 2

The express causes of action 3

The decisions below 6

Reasons for Granting the Writ 9

1. The "implied" remedy 9

2. Retroactivity 17

Conclusion 18

Appendix—

Opinion of the United States Court of Appeals for the District of Columbia Circuit, dated December 5, 1980 ..... 1a

Opinion of the United States District Court for the District of Columbia, dated November 20, 1978 .. 38a

PAGE

Order, dated March 4, 1981, denying petition for rehearing 64a

Order, dated March 4, 1981, denying rehearing *en banc* 66a

Provisions of the Securities Act of 1933, 15 U.S.C. § 77a *et seq.* (1976) 66a
Section 5, 15 U.S.C. § 77e 66a
Section 11, 15 U.S.C. § 77k 69a
Section 12, 15 U.S.C. § 77l 75a
Section 13, 15 U.S.C. § 77m 76a
Section 16, 15 U.S.C. § 77p 77a
Section 17, 15 U.S.C. § 77q 77a

Provisions of the Securities Exchange Act of 1934, 15 U.S.C. § 78a *et seq.* (1976) 79a
Section 9, 15 U.S.C. § 78i 79a
Section 10, 15 U.S.C. § 78j 83a
Section 18, 15 U.S.C. § 78r 84a
Section 28(a), 15 U.S.C. § 78bb(a) 85a

Table of Authorities

Cases:

Aaron v. *SEC*, 446 U.S. 680 (1980) 10, 14
Abrams v. *Johns-Manville Corp.*, [1979-80] CCH Fed. Sec.L.Rep. ¶ 97,305 (S.D.N.Y. 1980) 10n
Adams v. *Standard Knitting Mills, Inc.*, 623 F.2d 422 (6th Cir.), *cert. denied*, 101 S.Ct. 795 (1980) 10n
Affiliated Ute Citizens v. *United States*, 406 U.S. 128 (1972) 11

Blue Chip Stamps v. *Manor Drug Stores*, 421 U.S. 723 (1975) 10-11
Burks v. *Lasker*, 441 U.S. 471 (1979) 10

PAGE

Chevron Oil Co. v. *Huson*, 404 U.S. 97 (1971) 8-9, 17, 18
City of Philadelphia v. *Westinghouse Electric Corp.*, 210 F.Supp. 483 (E.D. Pa.), *petition for mandamus and prohibition denied*, 312 F.2d 742 (3d Cir. 1962), *cert. denied*, 372 U.S. 943 (1963) 14n
Clayton v. *Skelly Oil Co.*, [1977-78] CCH Fed.Sec.L. Rep. ¶ 96,269 (S.D.N.Y. 1977) 10n

Ernst & Ernst v. *Hochfelder*, 425 U.S. 185 (1976) 12, 14n

Forrestal Village, Inc. v. *Graham*, 551 F.2d 411 (D.C. Cir. 1977) 6, 8, 17

Heizer Corp. v. *Ross*, 601 F.2d 330 (7th Cir. 1979) 10n

International Brotherhood of Teamsters v. *Daniel*, 439 U.S. 551 (1979) 10

Kardon v. *National Gypsum Co.*, 69 F.Supp. 512 (E.D. Pa. 1946) 14n
Kissinger v. *Reporters Committee*, 445 U.S. 136 (1980) 14

Leist v. *Simplot*, 638 F.2d 564 (2d Cir. 1980), *cert. granted sub nom. New York Mercantile Exchange* v. *Leist* (No. 80-757), 49 U.S.L.W. 3617 (U.S. Feb. 23, 1981) 16

Poller v. *First Virginia Mortgage and REIT*, [1978] CCH Fed.Sec.L.Rep. ¶ 96,564 (E.D. Va. 1978) 9n

Ross v. *A.H. Robins Co.*, 607 F.2d 545 (2d Cir. 1979), *cert. denied*, 446 U.S. 946 (1980) 10n

PAGE

Santa Fe Industries, Inc. v. *Green*, 430 U.S. 462 (1977) 10
Seiffer v. *Topsy's International, Inc.*, 487 F.Supp. 653 (D.Kan. 1980) 10n
Superintendent of Insurance v. *Bankers Life and Casualty Co.*, 404 U.S. 6 (1971) 10-11

Touche Ross & Co. v. *Redington*, 442 U.S. 560 (1979) 7, 9, 11,13, 14n
Transamerica Mortgage Advisors, Inc. v. *Lewis*, 444 U.S. 11 (1979) 13, 15

Upjohn Co. v. *United States*, 101 S.Ct. 677 (1981) 14n

Valencia v. *Anderson Brothers Ford*, 617 F.2d 1278 (7th Cir.), *cert. granted* (No. 80-84), 49 U.S.L.W. 3350 (U.S. Nov. 10, 1980) 17

Congressional Documents:

H.R. Conf. No. 1838, 73d Cong., 2d Sess. (1934) 13

H.R. Rep. No. 2513, 84th Cong., 2d Sess. (1956) 15

Remarks of Rep. Rayburn, 78 Cong. Rec. 7701 (1934) 12

Remarks of Sen. Fletcher, 78 Cong. Rec. 2271 (1934) .. 14n

Stock Exchange Practices: Hearings on S.Res. 84, S.Res. 56 and S.Res. 97 Before Senate Comm. on Banking and Currency, 73d Cong., 2d Sess. (1934) 12, 12n

Stock Exchange Regulation: Hearing on H.R. 7852 and H.R. 8720 Before House Comm. on Interstate and Foreign Commerce, 73d Cong., 2d Sess. (1934) .. 12n

S.2693, 73d Cong., 2d Sess. (1934) 11

PAGE

Statutes:

Judicial Code, 28 U.S.C. § 1254(1) (1976) 2

Securities Act of 1933
§ 3(b), 15 U.S.C. § 77c(b) (Supp. III 1979) 15
§ 5, 15 U.S.C. § 77e (1976) 2, 3-4
§ 11, 15 U.S.C. § 77k (1976) 2, 4, 7, 13, 14, 15
§ 12, 15 U.S.C. § 77l (1976) 2, 4, 7, 13
§ 13, 15 U.S.C. § 77m (1976) 2, 5
§ 16, 15 U.S.C. § 77p (1976) 2, 5
§ 17, 15 U.S.C. § 77q (1976) ..... *passim*
§ 22, 15 U.S.C. § 77v (1976) 3

Securities Exchange Act of 1934
§ 9, 15 U.S.C. § 78i (1976) 2, 4, 5, 8
§ 10(b), 15 U.S.C. § 78j(b) (1976) ..... *passim*
§ 13(d), 15 U.S.C. § 78m(d) (1976 & Supp. III 1979) 3n
§ 13(e), 15 U.S.C. § 78m(e) (1976) 9
§ 14(a), 15 U.S.C. § 78n(a) (1976) 3n
§ 14(e), 15 U.S.C. § 78n(e) (1976) 9
§ 18, 15 U.S.C. § 78r (1976) 2, 5, 8, 11, 14
§ 27, 15 U.S.C. § 78aa (1976) 3
§ 28(a), 15 U.S.C. § 78bb (a) (1976) 2, 5

SEC—Regulation

17 C.F.R. § 240.10b-16 (1980) 9

Other Authorities:

Brooks, *The Go-Go Years* (1973) 2

No. 80-.....

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

PEAT, MARWICK, MITCHELL & CO.,
ANTHONY M. NATELLI and JOSEPH SCANSAROLI,

Petitioners,

v.

WACHOVIA BANK AND TRUST CO., N.A., MELLON BANK, N.A., FIRST WISCONSIN TRUST CO., THE DREYFUS OFFSHORE TRUST, N.V., and NATIONAL FIRE INSURANCE CO. OF HARTFORD,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Opinions Below

The opinion of the court of appeals (set forth beginning at page 1a of the appendix to this petition) is not yet officially reported; it is unofficially reported at [1980] CCH Fed.Sec.L.Rep. ¶ 97,712. The opinion of the district court (set forth beginning at page 38a of the appendix) is reported at 461 F.Supp. 999.

Jurisdiction

The judgment of the court of appeals was entered December 5, 1980. Petitioners' timely petition for rehearing,

with suggestion for rehearing *en banc*, was denied without opinion on March 4, 1981 (Circuit Judges Robb and MacKinnon would have heard the case *en banc* and Circuit Judge Wright did not participate) (66a-67a). This petition is filed within 90 days of that denial. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) (1976).

Statutory Provisions

Sections 5, 11, 12, 13, 16 and 17 of the Securities Act of 1933 (the "1933 Act"), 15 U.S.C. §§ 77e, 77k. 77l, 77m, 77p, 77q (1976), and Sections 9, 10, 18 and 28(a) of the Securities Exhange Act of 1934 (the "1934 Act"), 15 U.S.C. §§ 78i, 78j, 78r, 78bb(a) (1976), are set forth in the appendix beginning at page 68a.

Statement of the Case

National Student Marketing Corporation ("NSMC") was one of the "hot new issues" of the 1968-1969 stock market, chronicled in Brooks, *The Go-Go Years* (1973). Its stock was offered to the public in April 1968 at $6 and sold at $14 the same day. By December 1969, the stock, which had been split 2 for 1, was selling at $70, or 100 times earnings. Mr. Brooks explains that NSMC's president was able to fool "the whole brains trust of institutional investing" because "he was plausible and they were gullible as well as greedy; that, in times of speculative madness, the wisdom and experience of the soundest and soberest may yield to a hysteria induced by the glimpse of fool's gold dished by a young man with a smile on his lips and a gleam in his eye" (*id.* at 285).

In December 1969, Wachovia Bank and Trust Co., N.A., Mellon Bank, N.A., First Wisconsin Trust Co., The Drey-

fus Offshore Trust, N.V., and National Fire Insurance Co. of Hartford (collectively "Wachovia Bank") purchased some 130,000 shares of NSMC's stock from NSMC and two of its controlling persons. The purchase was made at a 37% discount from the market price of the stock. Within days, the market price began a precipitous decline and by the end of March 1970 had dropped by over 90%.

Peat, Marwick, Mitchell & Co. ("PMM") was the independent auditor of NSMC. PMM examined and reported upon the financial statements of NSMC which NSMC filed with the Securities and Exchange Commission ("SEC").*

Wachovia Bank sued NSMC, the selling shareholders, PMM and others in January 1973 and in 1975 added White & Case, counsel for NSMC in connection with the Wachovia Bank purchase, and its partner Epley as defendants. Wachovia Bank alleged that financial disclosures by NSMC including the financial statements examined and reported upon by PMM overstated NSMC's financial position and results of operations. The action asserted causes of action "implied" under § 17(a) of the 1933 Act and § 10(b) of the 1934 Act. The district court was alleged to have jurisdiction by reason of § 22 of the 1933 Act and § 27 of the 1934 Act.**

The express causes of action

Section 5 of the 1933 Act requires that securities sold by an issuer (including, for this purpose, controlling persons of an issuer) be registered with the SEC by a regis-

---

* Petitioners Natelli and Scansaroli were, respectively, a partner and an employee of PMM.

** Wachovia Bank also alleged causes of action "implied" under §§ 13(d) and 14(a) of the 1934 Act. The § 13(d) claim was abandoned (43a n.10), and Wachovia Bank did not appeal from the dismissal of the § 14(a) claim (8a n.6).

tration statement containing prescribed information including financial statements. Section 11(a)(3) provides an express damage remedy for purchasers of securities against the independent auditor in the event the financial statements contained in the registration statement are misleading.

Wachovia Bank contracted away that remedy. Wachovia Bank made representations in its stock purchase agreement concerning investment intent so that the transaction, as a "private placement", would be exempt from the registration requirement. Accordingly, no registration statement was filed.

Section 12(2) of the 1933 Act provides an express damage or rescission remedy for purchasers of securities (whether or not registered pursuant to § 5) if the securities are sold by means of a misleading statement. The purchaser's remedy is against the seller, not against other persons such as the independent auditor.

Other purchasers of NSMC stock brought a rescission action pursuant to § 12(2) against NSMC in March 1970. That action was later settled and the purchasers received back the stock they had exchanged for NSMC stock. Wachovia Bank did not utilize the § 12(2) remedy against NSMC or the selling stockholders from whom it purchased.

Section 9(a)(4) of the 1934 Act prohibits misleading statements by brokers and by sellers which are made for the purpose of inducing purchases of a security listed on an exchange, and § 9(e) provides an express damage remedy for persons who purchase such securities at a price affected by the misstatement. The stock of NSMC was not listed on a stock exchange.

Section 18 of the 1934 Act provides an express damage remedy for purchasers of securities, whether or not listed

on an exchange, against those, including the independent auditor, who make or cause to be made misleading statements which are contained in documents filed with the SEC. Reliance upon the misleading statement is an element of the cause of action.

Wachovia Bank has disclaimed any reliance upon the NSMC financial statements which were reported upon by PMM and which were filed with the SEC.*

Sections 13 of the 1933 Act and 18(c), as well as 9(e), of the 1934 Act require that any suit upon the express causes of action be brought within one year of discovery of the wrongful conduct or three years from the purchase complained of.

In early January 1970, within weeks of the stock purchase, internal counsel for one of the Wachovia Bank purchasers "turn[ed] the matter over to our counsel for litigation." The court of appeals held that equitable tolling of any limitations period insofar as PMM is concerned ended in February 1970. Wachovia Bank did not, however, bring suit until January 1973, 37 months after the purchase of the NSMC stock and at least 35 months after Wachovia Bank was on notice of a claim against PMM concerning the financial statements of NSMC.

Sections 16 of the 1933 Act and 28(a) of the 1934 Act provide that the express remedies of the Acts are in addition to any remedies available at common law. Wachovia Bank did not pursue any common law remedy against PMM.

PMM moved to dismiss the complaint on the grounds (i) that in the circumstances § 10(b) of the 1934 Act and

---

* The Wachovia Bank complaint pleaded reliance, but the courts below accepted Wachovia Bank's disclaimer of reliance made by affidavit in response to PMM's motion to dismiss.

§ 17(a) of the 1933 Act did not provide an "implied" damage remedy for Wachovia Bank and alternatively (ii) that under the ruling of the court of appeals in *Forrestal Village, Inc.* v. *Graham*, 551 F.2d 411 (D.C. Cir. 1977), the two-year statute of limitations of the District of Columbia "blue sky" law applied to such claims and barred Wachovia Bank's action commenced more than three years after its purchase.

The decisions below

The district court held that Wachovia Bank might assert "implied" causes of action under § 10(b) of the 1934 Act and § 17(a) of the 1933 Act since "it appears that neither § 18(a) [of the 1934 Act] nor § 12(2) [of the 1933 Act] provides the plaintiffs with adequate remedies" (47a). The district court, however, dismissed the complaint as time-barred (57a-62a).

The court of appeals affirmed the holding that Wachovia Bank has an "implied" damage remedy under § 10(b). The court declined to reach the question of whether Wachovia Bank has an "implied" remedy under § 17(a) of the 1933 Act (18a n.19).*

The court said that the inquiry concerning legislative intent is "not necessarily for evidence that Congress specifically intended to imply a private right of action, but rather for indications whether Congress meant to deny such a remedy" (21a). The court said that a § 10(b) damage remedy "compensates the investors," "affords a broad deterrent force against the fraud that the statute condemns" and is "a necessary supplement to administrative

---

* There can be little doubt but that under this Court's recent rulings there is no private damage remedy under § 17(a). Since it is difficult to distinguish § 10(b) from § 17(a), it was no doubt easier for the court of appeals not to deal with § 17(a).

enforcement" of the federal securities laws by the SEC (22a).

The court recognized that this Court has left open the question whether a cause of action may be implied under § 10(b) for actions and transactions which are the subject of express remedy provisions.

> "The Supreme Court has never decided whether the existence of express remedies precludes implication of a private right of action, and it specifically left the issue open in *Hochfelder,* 425 U.S. at 211 n.31, and in *Blue Chip Stamps,* 421 U.S. at 752 n.15. Dicta in *Redington* expressing reluctance to create an additional remedy when express remedies are already provided is [*sic*] not controlling in this case. In *Redington,* while the Court declined to decide the issue, *see* 442 U.S. at 574, it did note the existence of legislative history supporting a finding that the express remedies were intended to be exclusive, *see* 442 U.S. at 574." (28a n.29)

The court nevertheless and inexplicably said as to the legislative history referred to in *Touche Ross & Co.* v. *Redington,* 442 U.S. 560 (1979), that "no such evidence exists here" (28a n.29).

The court held that the express remedies could be ignored because such remedies were "not available" (34a) to Wachovia Bank: the express cause of action under § 11 of the 1933 Act was not available because "no registration statement was filed, and the suit was brought well beyond the time allowed under section 11" (29a); the express cause of action under § 12(2) of the 1933 Act was not available because of "section 12(2)'s short statute of limitations and apparent restriction of defendants to sellers" (31a); the

express cause of action under § 18 of the 1934 Act was not available because § 18 requires "actual reliance" (32a) and "plaintiffs have not claimed reliance" (34a). A § 18 cause of action also was time-barred under § 18(c). The court did not mention the express remedy of § 9(e) of the 1934 Act, which also was "not available." The court concluded:

> "Even if we were inclined to hold that the express remedies were intended to be exclusive, they should only preclude implied causes of action in those cases in which they truly constitute 'remedies.' . . ."
>
> • • •
>
> "Appellants should, therefore, be able to maintain a cause of action under section 10(b), the only true relief available to them." (33a, 35a)

In its reference to the "only true relief available to" Wachovia Bank, the court ignored the common law remedies available under state law.

In fashioning an "implied" federal remedy for Wachovia Bank the court eliminated the reliance and statute of limitations elements of the express federal remedies because those elements made the express remedies unavailable to Wachovia Bank. It said that the § 10(b) remedy "presumes reliance if the omission is material or if the misstatement affects the price of the stock" (32a), and it applied the local statute of limitations governing common law actions for fraud (14a) (although common law remedies were otherwise ignored).

The court of appeals reversed the dismissal of the Wachovia Bank action as time-barred, concluding that it was error to apply its decision in *Forrestal Village, supra,* "retroactively" to Wachovia Bank's action. Although it said the shorter "blue sky" statute "best furthered federal policy" (14a), it said that this second factor of *Chevron*

Oil Co. v. *Huson*, 404 U.S. 97 (1971), was "outweighed" by the first and third factors (13a). It held that, with the benefit of "equitable tolling" (15a-16a), the Wachovia Bank § 10(b) action was timely.

Reasons for Granting the Writ

1. *The "implied" remedy*—The court of appeals recognized how frequently this Court has been called upon to "decide whether a private remedy is implicit in a statute not expressly providing one," quoting from *Touche Ross & Co.* v. *Redington*, 442 U.S. at 562 (23a). It went on to say, however, and it is at the heart of its decision and why the writ should issue: "But the Court did not announce that it was going out of the business." (23a)

The court of appeals misunderstood or rejected the meaning of this Court's decisions, and it is not alone among the lower courts. The most recent weekly edition of the CCH Federal Securities Law Reports contains two decisions "implying" causes of action under § 13(e) of the 1934 Act and Rule 10b-16 under that Act; a third decision establishing a rule of damages in yet another "implied" action under § 14(e) of the 1934 Act; and a fourth decision fixing the amount of attorneys' fees in an "implied" action under § 10(b) of the 1934 Act. CCH Fed.Sec.L.Rep., Report No. 907 (April 1, 1981).

The writ should issue so that the lower courts may be reminded of the separation of legislative and judicial functions established by the Constitution and so that once and for all the existence and elements of "implied" remedies under §§ 10(b) and 17(a) may be settled.*

---

* The question has been the subject of mounting litigation in the lower courts. *See, e.g.*, the decisions cited by the court of appeals at 34a n.34, 28a n.28 and *Poller* v. *First Virginia Mortgage and*

The Court has three times expressly left open the question of whether there is an "implied" remedy under § 17(a) of the 1933 Act. Does § 17(a) "in light of the express civil remedies of the 1933 Act [give] rise to an implied cause of action," *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 734 n.6 (1975), or provide "private parties with an implied cause of action for damages," *International Brotherhood of Teamsters* v. *Daniel*, 439 U.S. 551, 557 n.9 (1979)? Most recently, in *Aaron* v. *SEC*, 446 U.S. 680, 689 (1980), the Court said "it has not had occasion to address the question whether a private cause of action exists under § 17(a)."

As to §10(b) of the 1934 Act, the Court has said that it has "recognized an implied cause of action under [§ 10 (b)] in some circumstances," *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 477 (1977). It has "assumed" the existence of the "implied" cause of action, *Aaron* v. *SEC*, 446 U.S. at 689, but "whether a cause of action exists" is a question the answer to which "may be assumed without being decided," *Burks* v. *Lasker*, 441 U.S. 471, 476 n.5 (1979).

The Court has never sustained the § 10(b) claim of a purchaser such as is present here. *Superintendent of Insurance* v. *Bankers Life & Casualty Co.*, 404 U.S. 6 (1971), involved an injured seller who has no remedy under the

---

REIT, [1978] CCH Fed.Sec.L.Rep. ¶ 96,564 at 94,352 (E.D.Va. 1978); *Clayton* v. *Skelly Oil Co.*, [1977-78] CCH Fed.Sec.L.Rep. ¶ 96,269 at n.1 (S.D.N.Y. 1977); *Abrams* v. *Johns-Manville Corp.*, [1979-80] CCH Fed.Sec.L.Rep. ¶ 97,305 (S.D.N.Y. 1980); *Seiffer* v. *Topsy's International, Inc.*, 487 F.Supp. 653, 662 (D.Kan. 1980).

For reasons which presumably include the settlement value of the mere existence of the issue, the issue has not often reached courts of appeals. *See*, however, *Adams* v. *Standard Knitting Mills, Inc.*, 623 F.2d 422, 429 n. 6 (6th Cir.), *cert. denied*, 101 S.Ct. 795 (1980); *Ross* v. *A.H. Robins Co.*, 607 F.2d 545 (2d Cir. 1979), *cert. denied*, 446 U.S. 946 (1980); *Heizer Corp.* v. *Ross*, 601 F.2d 330, 335 (7th Cir. 1979).

1933 Act, as did *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972).

The Court has not sustained an implied remedy which is broader than the remedy provided by Congress. To the contrary, in *Blue Chip Stamps*, 421 U.S. at 736, the Court said:

> "It would indeed be anomalous to impute to Congress an intention to expand the plaintiff class for a judicially implied cause of action [under § 10(b)] beyond the bounds it delineated for comparable express causes of action."

Similarly, in *Touche Ross & Co.* v. *Redington*, 442 U.S. at 574:

> "[W]e are extremely reluctant to imply a cause of action . . . that is significantly broader than the remedy that Congress chose to provide."

But the court below did exactly that, and it did so in the face of legislative history that demonstrates the importance Congress attached to the elements of the express causes of action.

In enacting § 18, Congress considered and rejected a cause of action based upon the effect upon market price of a report filed with the SEC, but the court of appeals here said that such an effect was sufficient for a § 10(b) claim (32a). The initial version of the provision which became § 18(a) required only that the plaintiff be a person "who shall have purchased or sold a security the price of which may have been affected by such statement." S. 2693, 73rd Cong., 2d Sess. § 17(a) (1934). That version was criticized in the hearings concerning the 1934 Act because it permitted recovery of damages by persons "who have not relied upon the inaccurate or misleading statement" and by those who

"trade recklessly" as well as "unscrupulous traders" who were not misled by the statements later alleged to be false.* Because of that criticism, the bill was redrafted and the requirement of actual reliance was added. As explained by Representative Sam Rayburn, then Chairman of the Committee on Interstate and Foreign Commerce:

> "The first provision of the bill as originally written was very much challenged on the ground that reliance should be required. This objection has been met." (78 Cong.Rec. at 7701 (1934))

The original version of § 18 also contained a provision barring any action not brought within two years after discovery of the facts constituting the cause of action and six years after the cause of action accrued. Senator Kean thought the two-year period "nothing but blackmail."

> "They discover it after the market has gone down, and after something has happened, and they are looking for mistakes. . . ." (*1934 Senate Hearings* at 6565)

The bill was revised to require that an action be brought within one year of discovery and three years of accrual of the cause of action. The Court has described this as a "significant" change, *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 212 n.31 (1976), but such a description is altogether too modest as the chronology of this action demonstrates.

As part of the same act passed in 1934, Congress also amended the 1933 Act to reduce the limitations period for

---

* *Stock Exchange Practices: Hearings on S.Res. 84, S.Res. 56 and S.Res. 97 Before Sen. Comm. on Banking and Currency*, 73d Cong. 2d Sess. at 6638, 7084 (1934) (*"1934 Senate Hearings"*); *Stock Exchange Regulation: Hearing on H.R. 7852 and 8720 Before House Comm. on Interstate and Foreign Commerce*, 73d Cong., 2d Sess. at 226, 656 (1934) (*"1934 House Hearing"*). *See also 1934 Senate Hearings* at 6939, 7186, 7567-68; *1934 House Hearing* at 262, 489.

actions under §§ 11 and 12 from two years from discovery and ten years from the purchase to one year and three years and to provide a limited reliance requirement in actions under § 11, *H.R. Conf. Rep. No. 1838,* 73d Cong., 2d Sess. 41-42 (1934).

"'Obviously, then, when Congress wished to provide a private damages remedy, it knew how to do so and did so expressly.'" *Transamerica Mortgage Advisors, Inc.* v. *Lewis,* 444 U.S. 11, 21 (1979), referring to § 18 of the 1934 Act and § 11 of the 1933 Act and quoting *Touche Ross & Co.* v. *Redington,* 442 U.S. at 572.

The court of appeals here stressed that the express remedies enacted by Congress were "not available" to Wachovia Bank (34a). It ignored this Court's direction in *Touche Ross,* 442 U.S. at 579, that:

> "[W]e are not at liberty to legislate. If there is to be a federal damages remedy under these circumstances, Congress must provide it. '[I]t is not for us to fill any *hiatus* Congress has left in this area.'"

The court of appeals rejected the *expressio unius* canon of statutory construction as "a dangerous road map" (27a). It ignored this Court's teaching in *Transamerica Mortgage,* 444 U.S. at 19-20, that:

> "[I]t is an elemental canon of statutory construction that where a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it. 'When a statute limits a thing to be done in a particular mode, it includes the negative of any other mode.' . . . See *Amtrak,* 414 U.S., at 458; *Securities Investor Protection Corp.* v. *Barbour,* 421 U.S. 412, 419; *T.I.M.E., Inc.* v. *United States,* 359 U.S. 464, 471,"

and that the *expressio unius* canon may yield only "to persuasive evidence of a contrary legislative intent." *Accord,*

Kissinger v. *Reporters Committee*, 445 U.S. 136, 148-49 (1980):

> "The Records Act also expressly provides administrative remedies for violations of the duties it imposes, implicating our conclusion in *Transamerica Mortgage* that it is 'an elemental canon of statutory construction that where a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it.'"

The intent of Congress with respect to private damage remedies is evident from the terms of the 1933 Act and the 1934 Act and from their legislative history. A federal damage remedy against experts such as independent auditors is provided where a statement or opinion of such a person is one which Congress required to be filed with the SEC—in § 11 for misstatements in 1933 Act registration statements and in § 18 for misstatements in 1934 Act filings. The legislative history demonstrates that a private damage action "was not within the contemplation of the Congress that enacted § 10(b)," *Aaron* v. *SEC*, 446 U.S. at 691.*

---

* Section 10(b) was intended, rather, to provide the *SEC* with authority to regulate new manipulative market devices not already expressly proscribed by other provisions of the 1934 Act, *Hochfelder*, 425 U.S. at 201-02. *See* 78 Cong. Rec. at 2271 (1934) (remarks of Sen. Fletcher).

An "implied" § 10(b) cause of action for an injured seller was first established in *Kardon* v. *National Gypsum Co.*, 69 F.Supp. 512 (E.D. Pa. 1946), decided by Judge Kirkpatrick, on the basis of the common law statutory tort concept emphatically rejected by the Court in *Touche Ross & Co.* v. *Redington*, 442 U.S. at 576-78. Judge Kirkpatrick also decided the first case to articulate the so-called "control group" test for determining the scope of the attorney-client privilege in the corporate context, *City of Philadelphia* v. *Westinghouse Electric Corp.*, 210 F.Supp. 483, 485 (E.D. Pa.), *petition for mandamus and prohibition denied*, 312 F.2d 742 (3d Cir. 1962), *cert. denied*, 372 U.S. 943 (1963). Only three months ago the Court considered and rejected that test, *Upjohn Co.* v. *United States*, 101 S.Ct. 677, 683 (1981).

Post-enactment legislative history provides, as it did in *Transamerica Mortgage*, 444 U.S. at 23 n.13, "another clear indication that Congress knew how to confer a private right of action when it wished to do so." In 1956 a bill was proposed in Congress to amend the 1933 Act to provide a civil remedy against experts such as the independent auditor for purchasers of publicly offered shares exempt from the 1933 Act registration requirements under § 3(b) (the exemption for small public offerings). The House Committee on Interstate and Foreign Commerce recommended passage of the amendment on the ground that purchasers in transactions exempt from the registration requirement, like the Wachovia Bank purchase, may rely on "statements of officers and directors of the issuer, its underwriters, accountants, attorneys, engineers and other experts" and "there is no civil liability to any of the aforementioned individuals," *H.R. Rep. No. 2513*, 84th Cong., 2d Sess. at 5 (1956).

> "The only civil remedy the purchaser of a security, issued pursuant to section 3(b) exemption, has for false and misleading statements or omissions in [an] offering circular is to sue the seller of the security under section 12 [of the 1933 Act]. By contrast, the investor in registered securities has civil remedies under sections 11 and 12 . . . [and] can sue not only the seller of the security, but also the issuer, its officers and directors, the underwriters, the accountants, the attorneys." (*Ibid.*)

The SEC opposed the amendment since it would frustrate the purpose of the exemption from registration, and "criminal liability in the event that false statements were made" constituted a sufficient deterrent to non-sellers (*id.* at 32). The SEC recognized § 17 of the 1933 Act provides

only for criminal and injunctive remedies, that the § 11 cause of action for money damages was not applicable and that the § 12(2) cause of action for money damages was available only against sellers (*id.* at 31). It said "[t]he history of the statute makes it clear that this pattern of the statute was based on a policy decision of the Congress" concerning liability "in the exempted field" (*ibid.*). The bill was not enacted.

The court of appeals did not refer to the legislative history at the time of the enactment of the 1933 and 1934 Acts. Rather, it argued that the absence of express Congressional disapproval of "judicial implication" was a "significant" silence (36a), relying upon *Leist* v. *Simplot*, 638 F.2d 283 (2d Cir. 1980). This Court has granted certiorari to review that decision *sub nom. New York Mercantile Exchange* v. *Leist* (No. 80-757), 49 U.S.L.W. 3617 (U.S. February 23, 1981).

The court's acknowledgment that "judicial implication" is what is involved underlines the error it made. The Constitution prohibits "judicial implication" of private causes of action. Congressional silence does not validate the exercise by federal judges of Congress' legislative power.

As is evidenced by the decision below and by the decisions referred to earlier (*supra* p. 9), many lower courts are reluctant to follow the teaching of this Court's most recent decisions concerning the inference of a private remedy from a statute providing none. Unstated, but plainly underlying that reluctance, is the belief that the federal courts must provide a forum and a remedy for every grievance that has some relationship to federal legislation or regulation. Only this Court can recall the lower courts to their role under the Constitution.

2. *Retroactivity*—The decision of the court of appeals denying retroactive application to its ruling in *Forrestal Village* is in direct conflict with *Valencia* v. *Anderson Brothers Ford*, 617 F.2d 1278 (7th Cir.), *cert. granted* (No. 80-84), 49 U.S.L.W. 3350 (U.S. Nov. 10, 1980).

There, the Court of Appeals for the Seventh Circuit held:

> "All three of the factors listed in *Chevron Oil* must be shown to favor prospective-only application before a decision will be denied retroactive effect." (617 F.2d at 1289)

Here, referring to the second factor of *Chevron Oil*, the court below said:

> "The second factor is more equivocal. The court did base its decision in *Forrestal Village* on which statute of limitations period best furthered federal policy. But the choice was ultimately dictated by the 'commonality of purpose' between the blue sky law and sections 10(b) and 17(a), 551 F.2d at 414, not by any substantive difference between a two- and three-year limitation. Even if this second factor suggests retroactive application of *Forrestal Village*, we think it outweighed by the first and third criteria, which overwhelmingly dictate that the decision be applied prospectively here." (13a-14a) (footnote omitted)

Even as to the first and third *Chevron Oil* factors, the court's certitude is contradicted by its own *Forrestal Village* decision where, in applying the "blue sky" statute of limitations to bar the plaintiff, it had said the result was "obvious" (551 F.2d at 414). An obvious result can be neither unforeseeable nor inequitable.

In any case, the plaintiff in *Forrestal Village* was held to be time-barred by the two year "blue sky" statute. What

then was different about the situation of the Wachovia Bank plaintiffs who turned the matter over to counsel for litigation more than three years before they brought suit?

Unless the presence of all three *Chevron Oil* factors is required, the precedential value of any decision is uncertain. The decision below made of the rule of *Chevron Oil* not a rule, but the present-day equivalent of the length of the chancellor's foot.

CONCLUSION

The writ of certiorari should issue.

Respectfully submitted,

William E. Hegarty
80 Pine Street
New York, New York 10005
(212) 825-0100

Counsel of Record

Victor M. Earle, III
345 Park Avenue
New York, New York 10022

Attorneys for Petitioners

Of Counsel:

Mathias E. Mone
Joseph W. Muccia
Cahill Gordon & Reindel
80 Pine Street
New York, New York 10005

April 1981

APPENDIX

Opinion of United States Court of Appeals

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 79-1595

WACHOVIA BANK AND TRUST CO., N.A.
(as Trustee and Agent for various
trust accounts), ET AL., APPELLANTS

v.

NATIONAL STUDENT MARKETING CORPORATION, ET AL.

No. 79-1596

WACHOVIA BANK AND TRUST CO., N.A.
(as Trustee and Agent for various
trust accounts), ET AL., APPELLANTS

v.

NATIONAL STUDENT MARKETING CORPORATION, ET AL.

No. 79-1597

WACHOVIA BANK AND TRUST CO., N.A.
(as Trustee and Agent for various
trust accounts), ET AL.

v.

NATIONAL STUDENT MARKETING CORPORATION, ET AL.
WHITE & CASE, ET AL., APPELLANTS

Opinion of United States Court of Appeals

No. 79-1598

WACHOVIA BANK AND TRUST CO., N.A.
(as Trustee and Agent for various
trust accounts), ET AL.

v.

NATIONAL STUDENT MARKETING CORPORATION, ET AL.
PEAT, MARWICK, ET AL., APPELLANTS

No. 79-1599

WACHOVIA BANK AND TRUST CO., N.A.
(as Trustee and Agent for various
trust accounts), ET AL.

v.

NATIONAL STUDENT MARKETING CORPORATION, ET AL.
ROGER O. WALTHER, APPELLANT

No. 79-1600

WACHOVIA BANK AND TRUST CO., N.A.
(as Trustee and Agent for various
trust accounts), ET AL.

v.

NATIONAL STUDENT MARKETING CORPORATION, ET AL.
JAMES F. JOY, APPELLANT

Opinion of United States Court of Appeals

No. 79-1601

WACHOVIA BANK AND TRUST CO., N.A.
(as Trustee and Agent for various
trust accounts), ET AL.

v.

NATIONAL STUDENT MARKETING CORPORATION, ET AL.
DONALD A. FERGUSSON AND ROBERT A. FERGUSSON,
APPELLANTS

No. 79-1602

WACHOVIA BANK AND TRUST CO., N.A.
(as Trustee and Agent for various
trust accounts), ET AL.

v.

NATIONAL STUDENT MARKETING CORPORATION, ET AL.
CORTES W. RANDELL, APPELLANT

Appeals from the United States District Court
for the District of Columbia

(D.C. Civil Action No. 166-73)

Argued December 13, 1979

JUDGMENT ENTERED THIS DATE
Decided December 5, 1980

Juan A. del Real and *Gilbert C. Miller,* with whom *Richard M. Phillips* was on the brief, for appellants in No. 79-1595.

Paul Gonson, Principal Associate General Counsel, Securities and Exchange Commission, with whom *Michael K. Wolensky,* Assistant General Counsel, Securities and Exchange Commission, was on the brief, for amicus curiae, Securities and Exchange Commission, in No. 79-1595 urging reversal.

Milton V. Freeman, with whom *Daniel A. Rezneck, Thomas D. Nurmi,* and *Lawrence A. Schneider* were on the brief, for White & Case and Marion Jay Epley, III, appellees in No. 79-1595 and cross-appellants in No. 79-1597.

William E. Hegarty, with whom *Mathias E. Mone* was on the brief, for Peat, Marwick, Mitchell & Co., et al. appellees in Nos. 79-1595 and 79-1596 and cross-appellants in No. 79-1598.

Franklin M. Schultz and *Bruce W. Dunne* were on the brief for James F. Joy, appellee in Nos. 79-1595, 79-1596, 79-1597, 79-1598, 79-1599, 79-1601, and 79-1602 and cross-appellant in No. 79-1600.

Sidney Dickstein was on the brief for Roger O. Walther, appellee in Nos. 79-1595, 79-1596, 79-1597, 79-1598, 79-1600, 79-1601, and 79-1602 and cross-appellant in No. 79-1599.

William R. Bernard was on the brief for Cortes W. Randell, appellee in Nos. 79-1595, 79-1596, 79-1597, 79-1598, 79-1599, 79-1600, and 79-1601 and cross-appellant in No. 79-1602.

George P. Michaely, Jr., and *Thomas W. Armstrong* were on the brief for Fergusson, et al., appellees in No. 79-1595 and cross-appellants in No. 79-1601.

Also *Cherif Sedky* entered an appearance for appellants Wachovia Bank and Trust Co., et al. in Nos. 79-1595 and 79-1596.

Opinion of United States Court of Appeals

Before: ROBINSON and MIKVA, *Circuit Judges*, and FLANNERY*, *United States District Judge* for the District of Columbia.

Opinion for the court filed by *Circuit Judge* MIKVA.

MIKVA, *Circuit Judge*: This is yet another installment in the saga of the collapse of one of the glamor stocks of the 1960s, the National Student Marketing Corporation (NSMC). Appellants allege a widespread scheme to misrepresent the financial condition of NSMC and thereby to stimulate investor interest in NSMC's securities. They seek damages to remedy losses suffered when the value of NSMC stock dropped suddenly and dramatically more than a decade ago, and they appeal the district court's dismissal of their claim as time-barred. On cross-appeal, defendants argue that the court below erred in finding that appellants have a private right of action under section 10(b) of the Securities Exchange Act of 1934 (the 1934 Act), 15 U.S.C. § 78j(b) (1976), and under section 17(a) of the Securities Act of 1933 (the 1933 Act), 15 U.S.C. § 77q(a) (1976).

We reverse the district court's holding that appellants' claims are barred by the statute of limitations, and we affirm appellants' right to pursue a remedy under section 10(b) of the 1934 Act.

I. BACKGROUND

In December of 1979, appellants (Wachovia)[1] bought approximately five million dollars' worth of NSMC stock

---

* Sitting by designation pursuant to 28 U.S.C. § 292(a). Judge Flannery authored section II of this opinion.

[1] Appellants are the Wachovia Bank and Trust Co., the Mellon Bank, the First Wisconsin Trust Co., the Dreyfus Offshore Trust, and the National Fire Insurance Company of Hartford.

from the corporation and two of its directors. The purchase was a private placement transaction governed by detailed purchase agreements. Two months later, the market price of NSMC stock declined more than sixty percent, and NSMC announced that it expected to report a loss for the previous fiscal quarter.

The Securities and Exchange Commission (SEC) then began a two-year investigation of NSMC, which ended in February, 1972, with the filing of an enforcement and injunction action against NSMC and the other major participants in NSMC's merger with Interstate National Corporation.[2] The Commission charged that the price of NSMC stock had been artificially inflated in violation of the securities laws. In addition, various civil actions were filed in 1970 and 1972 by purchasers of NSMC stock.[3]

The original complaint in this case, filed January 29, 1973, sought damages from NSMC and several of its officers and employees and from Peat, Marwick, Mitchell & Co. (PMM), NSMC's independent auditor; Anthony Natelli, the PMM partner in charge of the NSMC account; and Joseph Scansaroli, the PMM audit supervisor. These defendants were charged with participating in a conspiracy to defraud investors by artificially inflating the price of NSMC stock and thereby violating various sections of the 1933 and 1934 Acts. Specifically, appellants contended that

---

[2] *SEC v. National Student Marketing Corp.*, 457 F. Supp. 682 (D.D.C. 1978).

[3] *Natale v. National Student Marketing Corp.*, Civ. No. 72-721 (S.D.N.Y., filed Feb. 18, 1972); *Lipsig v. National Student Marketing Corp.*, Civ. No. 70-2006 (S.D.N.Y., filed May 15, 1970); *Stuckey v. National Student Marketing Corp.*, Civ. No. 70-H-251 (S.D. Tex., filed March 19, 1970); *Garber v. Randell*, Civ. No. 70-835 (S.D.N.Y., filed March 2, 1970).

misrepresentations about NSMC's financial condition had been included in oral statements, in press releases, in reports filed with the SEC, and in other published reports not filed with the Commission. The fraudulent scheme was allegedly furthered by NSMC's acquisition of a number of corporations.

The original complaint did not name as defendants White & Case, NSMC's outside counsel, or Jay Epley, the White & Case partner principally in charge of the NSMC account. As NSMC's counsel, they had drafted a purchase agreement between appellants and NSMC and had issued a legal opinion to appellants, in which the buyers were assured that the contemplated transaction would not violate any statute. Two days before the complaint was filed, appellants had entered into a letter agreement with White & Case and Epley, which provided that the statute of limitations would be tolled as to them for two years from the date of the letter. Appellants then amended their complaint on May 28, 1975, to include White & Case and Epley as defendants.

The defendants[4] moved to dismiss the complaint on two grounds: that the action was time-barred under the two-year statute of limitations of the District of Columbia's blue sky law, and that the sections of the securities acts on which the claims were based did not provide for or allow a private right of action. The district court held that a private remedy was implied under section 10(b) of the 1934

---

[4] Appellants settled with NSMC and various named defendants, and all claims against those parties were dismissed. Defendants below, and appellees here, are PMM and Natelli and Scansaroli; White & Case and Epley; and the following NSMC officers and directors: John G. Davies, James F. Joy, Dennis M. Kelly, Bernard J. Kurek, Cortes W. Randell, and Roger O. Walther.

Act and under section 17(a) of the 1933 Act, but the court dismissed the action as untimely.[5] Both issues are now before this court.[6]

II. Statute of Limitations

Two statute of limitations questions must be resolved: (1) whether the district court committed error in applying retrospectively *Forrestal Village, Inc. v. Graham,* 551 F.2d 411 (D.C. Cir. 1977), which calls for a two-year statute of limitations in Rule 10b-5 actions; and (2) whether the district court properly declined application of the equitable tolling principle.[7]

---

[5] The district court's opinion is reported at 461 F. Supp. 999 (D.D.C. 1978).

[6] Appellants abandoned their claim under § 13(a) of the 1934 Act, 15 U.S.C. § 78m(a) (1976). Their claim under § 14(a) of that Act, 15 U.S.C. § 78n(a) (1976), was dismissed by the court below, and appellants do not appeal from that decision. In addition, defendants-appellees John J. Davies, Dennis M. Kelly, and Bernard J. Kurek have not joined the cross-appeal.

[7] A third issue—whether appellants may take advantage of class action tolling—warrants only brief comment. In *American Pipe & Construction Co. v. Utah,* 414 U.S. 538 (1974), the Supreme Court held that commencement of a class action tolls the running of the statute of limitations "for all purported members of the class who make timely motions to intervene after the court has found the suit inappropriate for class action status." *Id.* at 553. Hence, a member of the purported class, after denial of certification, may intervene in an individual suit without penalty for the time period during which the class certification issue is pending.

The district court correctly ruled that appellants fail to qualify for the *American Pipe* tolling rule. Here, certification of the class was granted, not denied. Moreover, no intervention was ever attempted; appellants filed their own action nine months before the district court granted certification, and preferred to pursue their own case rather than seek class relief.

A. *The Applicable Statute of Limitations*

For causes of action implied under the securities laws, the forum state's statute of limitations rules. *See Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 210 n.29 (1976). At issue here is which limitations period to apply: the three-year general fraud provision, D.C. Code § 12-301(8) (1973), or the two-year blue sky law provision, *id.* § 2-2413(e).

Resolution of this issue determines whether this suit should be dismissed on statute of limitations grounds. Appellants bought NSMC stock on December 17, 1969. The statute of limitations began to run at the end of February, 1970,[8] and the suit was filed in January, 1973—more than two years, but less than three years, after the limitations period had begun to run. The district court found the two-year period applicable and accordingly dismissed the case for untimely filing.

The question of the appropriate statute of limitations is an equivocal one because the trend in the federal case law has shifted. Federal courts once favored invocation of the general fraud limitations period for Rule 10b-5 actions. But during the last decade, the law has moved toward application of the blue sky law limitations period.

The case law in this circuit reflects that general trend. Before 1977, this court favored application of the three-year general fraud limitations period. But in *Forrestal Village, Inc. v. Graham*, 551 F.2d 411 (D.C. Cir. 1977), we decided that the two-year blue sky law provision, rather than the three-year general fraud limitations guideline, " 'best effectuates the federal policy involved.' " *Id.* at

[8] We arrive at this date by invoking the doctrine of equitable tolling. *See* section II(B) *infra*.

413.[9] In so ruling, this circuit joined the majority of circuits, which at that time—in 1977—applied local blue sky law limitations periods to section 10(b) and section 17(a) securities actions.

Whether the instant case should be governed by a three-year or two-year statute of limitations thus turns on whether the *Forrestal Village* decision is applied prospectively or retrospectively. The critical precedent on this question is *Chevron Oil Co. v. Huson,* 404 U.S. 97 (1971). We therefore look to that opinion for guidance.

In *Chevron,* the plaintiff, who was injured while working on a drilling rig located on the Outer Continental Shelf, filed suit more than two years after the date the injury occurred. The defendant originally declined to raise the issue of the limitations period. The parties correctly assumed, based on federal court precedent, that admiralty law—including the doctrine of laches—applied to the case.[10] During discovery, however, the Supreme Court released its decision in *Rodrigue v. Aetna Casualty & Surety Co.,* 395 U.S. 352 (1969), which removed the applicability of admiralty law to cases like *Chevron.* Based on *Rodrigue,* the district court in *Chevron* applied the local one-year limitations period for personal injury suits and, accordingly, dismissed the case. *See* 404 U.S. at 98-99.

Articulating three criteria, the Supreme Court ruled in *Chevron* that its *Rodrigue* decision should be given prospective effect. The first, and most fundamental, factor is that "the decision to be applied nonretroactively must es-

---

[9] *Forrestal Village* noted that the blue sky statute, because it deals with the sale of securities, more closely resembles Rule 10b-5 than does common law fraud. *See* 551 F.2d at 414.

[10] The plaintiff alleged that, only many months after the accident occurred, did he realize the serious nature of the injury.

tablish a new principle of law, either by overruling clear past precedent on which litigants may have relied or by deciding an issue of first impression whose resolution was not clearly foreshadowed." *Id.* at 1006 (citation omitted). Second, the court must consider whether retrospective application will further or hinder the purpose of the decision in question. Finally, prospectivity is required if retroactive application will create substantial injustice.

In applying the first criterion and deciding whether a current decision overrules precedent, does the court look to the law as it appears at the time of the new decision, or to the time when a claim arose and a plaintiff relied on the law? The state of the law may fluctuate between these two dates, thereby changing the outcome of the first inquiry required by *Chevron*. The distinction is critical here.

The court below applied *Forrestal Village* retroactively. It ruled that that case failed to overrule precedent, as it existed when the decision was released in 1977. It is correct that, in 1977, the circuits favored application of the blue sky law limitations period. *Chevron*, however, does not seek to compare a new decision to the extant law when that decision was published. Rather, *Chevron* favors comparing the decision to the law at the time the plaintiff relied upon it, that is, the law after the claim arose and during the running of the limitations period.

This choice is clear in the opinion itself. The very language of the first criterion set out in *Chevron* requires nonretroactive application of a decision that overrules law "on which litigants may have relied." Moreover, the Court repeatedly noted that its *Rodrigue* decision reversed the law that the plaintiff relied upon when he contemplated filing suit. For example, the Court observed that, from the time the plaintiff was injured until he commenced suit, the

federal cases supported application of admiralty law to cases such as plaintiff's: "[i]t cannot be assumed that he [plaintiff] did or could foresee that this consistent interpretation of the Lands Act would be overturned. The most he could do was rely on the law as it then was." *Id.* at 107. In reciting the facts, the Court remarked, "[w]hen this law suit was initiated, there was a line of federal court decisions" favoring application of admiralty law, and the doctrine of laches, to the case. *Id.* at 99. The court further noted that the plaintiff's injuries occurred three years before *Rodrigue* was released, and that the plaintiff filed his law suit more than one year before that decision.

The lesson is clear. *Chevron* mandates nonretroactive application of a statute of limitations decision that overrules the weight of past precedent. In deciding whether this criterion is met, a court must compare the new limitations ruling with the law the plaintiff relied upon when he contemplated filing suit. The court below thus erred in looking at the state of the law in 1977 when *Forrestal Village* was decided.

Appellants relied on the law from December, 1969, when they bought NSMC stock, until January, 1973, when they filed suit. During that period, this circuit favored application of the general fraud limitations period. In fact, courts in this circuit reaffirmed the three-year fraud period as late as 1975. *See, e.g., Vance v. National Realty Trust,* [1974-1975 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,004 (D.C. Cir. 1975); *National Realty Trust v. Neelon Management Co.,* [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,049 (D.D.C. 1973); *Conlon v. University Computing Co.,* [1972-1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 93,796 (D.D.C. 1973).

Moreover, as of December, 1971—when the two-year limitations deadline applied by the district court expired—only one circuit court and one federal district court had applied the blue sky law limitations period to federal securities actions. *See Vanderboon v. Sexton,* 422 F.2d 1233 (8th Cir. 1970); *Batchelor v. Legg & Co.,* 52 F.R.D. 533 (D. Md. 1971). On the other hand, forty-six federal court decisions had applied the forum state's general fraud statute of limitations.[11] These cases included opinions from eight United States Circuit Courts of Appeals.[12]

Thus, prior to, and during, the running of the limitations period, federal courts, including this circuit, overwhelmingly adopted the general fraud limitations period. It was the law at this point in time on which appellants relied. Accordingly, consideration of the first factor of *Chevron* points toward prospective application of *Forrestal Village.*

For the same reason, the third criterion also favors prospectivity. As in *Chevron,* "[i]t would also produce the most 'substantial inequitable results' to hold that [appellants] 'slept on [their] rights' at a time when [they] could not have known the time limitation that the law imposed upon [them]." 404 U.S. at 108 (citation omitted).

The second factor is more equivocal. The court did base its decision in *Forrestal Village* on which statute of limita-

---

[11] *See* Brief for Appellants at 34 n.22.

[12] *E.g., Richardson v. MacArthur,* 451 F.2d 35 (10th Cir. 1971); *Bailes v. Colonial Press, Inc.,* 444 F.2d 1241 (5th Cir. 1971); *Douglass v. Glenn E. Inton Investments, Inc.,* 440 F.2d 912 (9th Cir. 1971); *Klein* v. *Auchincloss, Parker & Redpath,* 436 F.2d 339 (2d Cir. 1971); *Morgan v. Koch,* 419 F.2d 993 (7th Cir. 1969); *Charney v. Thomas,* 372 F.2d 97 (6th Cir. 1967); *Janigan v. Taylor,* 344 F.2d 781 (1st Cir.), *cert. denied,* 382 U.S. 879 (1965); *Stevens v. Abbott, Proctor & Paine,* 288 F. Supp. 836 (E.D. Va. 1968); *Tobacco & Allied Stocks v. Transamerica Corp.,* 143 F. Supp. 323 (D. Del. 1956).

tions period best furthered federal policy. But the choice was ultimately dictated by the "commonality of purpose" between the blue sky law and sections 10(b) and 17(a), 551 F.2d at 414, not by any substantive difference between a two- and three-year limitation. Even if this second factor suggests retroactive application of *Forrestal Village,* we think it outweighed by the first and third criteria, which overwhelmingly dictate that the decision be applied prospectively here.[13] This action is therefore guided by the three-year statute of limitations for general fraud.

B. *Equitable Tolling*

The doctrine of equitable tolling permits, with respect to fraud, the tolling of the limitations period until the plaintiff discovers, or should have discovered through the exercise of due diligence, the fraudulent activity. This court recently articulated the equitable tolling standard in *Fitzgerald v. Seamans,* 553 F.2d 220, 228 (D.C. Cir. 1977): "time does not begin to run until plaintiff discovers, or by reasonable diligence could have discovered, the basis of

---

[13] Appellees' citation to *Zweibon v. Mitchell,* 606 F.2d 1172, 1177 (D.C. Cir. 1979), *petition for cert. filed,* 48 U.S.L.W. 3404 (U.S. Dec. 7, 1979) (Nos. 79-881 & 79-883), for the proposition that "[r]etroactivity is the rule" is unavailing. In *Zweibon,* the judicial ruling at issue—requiring a warrant for domestic national security wiretaps—did not overrule precedent. Nor was the ruling unforeshadowed. On several occasions in the late 1960s, the Supreme Court had expressed concern regarding warrantless wiretaps, and "[e]xtension of that concern to the national security sphere was certainly likely, though perhaps not inevitable." *Id.* at 1178 n.31. Hence, rather than adopt an avulsive change in the law, or resolve a complex issue of first impression, *Zweibon* merely extended existing law to domestic national security situations. However, where, as here, a decision displaces the weight of precedent relied upon by the plaintiff, prospective, rather than retrospective, application must be the rule.

the lawsuit." The *Fitzgerald* formulation of the equitable tolling doctrine reiterated a standard long applied in federal courts. *See, e.g., Cook v. Avien, Inc.*, 573 F.2d 685, 695 (1st Cir. 1978); *Berry Petroleum Co. v. Adams & Peck*, 518 F.2d 402, 410 (2d Cir. 1975); *Klein v. Bower*, 421 F.2d 338, 343 (D.C. Cir. 1970).

The district court decided against invocation of the equitable tolling principle. It ruled that appellants "should have known of the fraud within the two-year statute of limitations, running immediately after the sale." 461 F. Supp. at 1010. The court based its ruling on certain " 'code blue' notices of fraud." *Id.* at 1009. These included the precipitous decline of the price of NSMC stock between December 17, 1969, and February 17, 1970; NSMC's reported loss on February 16, 1970, of 1.2 to 1.7 million dollars; and articles in *Barron's* (December 22, 1969)[14] and *The Wall Street Journal* (February 17, 1970),[15] questioning NSMC's auditing procedures and reporting the company's financial problems. The court below thus concluded:

> [T]hese facts, coupled with the several lawsuits filed in 1970, provided a clearly marked trail, which, if pursued with diligence, would have led the plaintiffs to the fraud of the NSMC officials and to the attorney-defendants and their involvement in the stock sale.

Id.

There can be little doubt that these code blue factors implicated the accountant-defendants—but only in February, 1970, when most of the events occurred. The only hint of fraud available to appellants before February, 1970, was

---

[14] Joint Appendix (J.A.) at 710.

[15] J.A. at 712.

the publication of the *Barron's* article, which appeared on December 22, 1969. This article criticized NSMC's practices of deferring costs, and of including as part of its 1969 income the earnings of companies acquired after expiration of the 1969 fiscal year.

This article, taken alone, was insufficient to alert appellants to fraudulent activity committed by the accountant-defendants. Although the article questions the nature of certain accounting procedures, it in no way intimates that such procedures were fraudulent. As a matter of law, we believe that one article challenging the accounting procedures of a reputable firm is insufficient to impute knowledge of fraud to appellants. *See Robertson v. Seidman & Seidman*, 609 F.2d 583 (2d Cir. 1979) (publicly disseminated information doubting propriety of accounting practices inconclusive regarding time that plaintiff possessed knowledge of fraud). Hence, although we agree with the court below that the code blue factors, taken cumulatively, were sufficient to warn appellants of the possibility of fraud on the part of the accountant-defendants, we nonetheless find that the court committed error in declining to toll the limitations period until February, 1970. The statute of limitations cannot run until the events that implicated the accountants occurred, and all but one of them occurred, or became discernible, in February, 1970. The statute of limitations against the accountants should thus be tolled until that time. Given our holding above that the three-year statute of limitations applies to this case, appellants filed this suit against the auditor-defendants within the limitations period.

We are unsure whether the code blue factors were sufficient to place appellants on notice in February, 1970, of the possibility of fraud committed by the attorney-defen-

dants. But a more precise determination on the running of the limitations period against these defendants is unnecessary. Insofar as the three-year statute of limitations applies, and February, 1970, is the earliest possible time the attorney-defendants could have been implicated, appellants' claims against these defendants clearly fall within the limitations deadline. We therefore reverse the ruling of the court below and find that appellants' claims are not time-barred.

III. Availability of Implied Remedies

The second issue in this case resurrects a decade-old and multi-faceted controversy and requires application of a doctrine that was examined by the Supreme Court no less than five times during the last Term. The question before the court on the cross-appeal, and necessary to our decision in light of our holding on the statute of limitations question, is whether an implied right of action is available to Wachovia under section 10(b) of the 1934 Act[16] and the corresponding SEC Rule 10b-5,[17] as well as under section

---

[16] It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

. . . .

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Section 10(b), 15 U.S.C. § 78j(b) (1976).

[17] Rule 10b-5, promulgated by the SEC pursuant to authority granted by § 10(b) of the 1934 Act, provides in full:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate com-

17(a) of the 1933 Act,[18] or whether plaintiffs are limited to the express remedies set forth in those statutes.[19]

---

merce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5 (1979).

[18] It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 17(a), 15 U.S.C. § 77q(a) (1976).

[19] Because we decide that appellants may pursue a private remedy under § 10(b) of the 1934 Act, and because their claims can be fully satisfied by such an action, we do not decide whether a private right of action may be implied under § 17(a) of the 1933 Act. That question has explicitly been left open by the Supreme Court. *See Aaron v. SEC*, 100 S. Ct. 1945, 1951 (1980); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 733 n.6 (1975). The courts of appeals are in conflict on this issue, though most have recognized a cause of action implicit in § 17(a). *Compare Kirshner v. United States*, 603 F.2d 234, 241 (2d Cir. 1978), *cert. denied*, 442 U.S. 909 (1979) (recognizing implied remedy under § 17(a)); *Daniel v. International Bhd. of Teamsters*, 561 F.2d 1223, 1245-46 (7th Cir.

A. *Implying a Cause of Action Under Section 10(b) and Rule 10b-5*

It has been almost thirty-five years since a private cause of action was first implied under section 10(b) and Rule 10b-5, and "a substantial body of case law and commentary has developed as to its elements." *Ernst & Ernst v. Hochfelder,* 425 U.S. 185, 197 (1976). Although the initial formulation of the implied remedy and the molding of its contours occurred in the courts of appeals,[20] the Supreme Court has recognized an implied cause of action under 10(b) many times.[21]

Moreover, despite many efforts, successful and unsuccessful, to amend related sections of the national securities laws, Congress never saw reason to limit or constrict the application of implied remedies under section 10(b). Long-

---

1977), *rev'd on other grounds,* 439 U.S. 551 (1979) (same); *Newman v. Prior,* 518 F.2d 97, 99 (4th Cir. 1975) (same), *with Shull v. Dain, Kaiman & Quail, Inc.,* 561 F.2d 152, 159 (8th Cir. 1977), *cert. denied,* 434 U.S. 1086 (1978) (rejecting implied remedy).

[20] *See, e.g., Matheson v. Armbrust,* 284 F.2d 670 (9th Cir. 1960); *Hooper v. Mountain States Securities Corp.,* 282 F.2d 195 (5th Cir. 1960), *cert. denied,* 365 U.S. 814 (1961); *Fratt v. Robinson,* 203 F.2d 627 (9th Cir. 1953); *Fischman v. Raytheon Mfg. Co.,* 188 F.2d 783 (2d Cir. 1951).

[21] *See Santa Fe Indus., Inc. v. Green,* 430 U.S. 462, 477 (1977); *Piper v. Chris-Craft Indus., Inc.,* 430 U.S. 1, 25 (1977) ("This Court has nonetheless held that in some circumstances a private cause of action can be implied with respect to the 1934 Act's anti-fraud provisions, even though the relevant provisions are silent as to remedies."); *Hochfelder,* 425 U.S. at 196 ("[T]he existence of a private cause of action for violations of the statute and the Rule is now well-established."); *Blue Chip Stamps v. Manor Drug Stores,* 421 U.S. 723, 730 (1975); *Affiliated Ute Citizens v. United States,* 406 U.S. 128, 144-54 (1972); *Superintendent of Ins. v. Bankers Life & Casualty Co.,* 404 U.S. 6, 13 n.9 (1971) ("It is now well established that a private right of action is implied under § 10(b).").

standing judicial application of a court's statutory interpretation, the Supreme Court has said, when added to the failure of Congress to reject its reasoning, "argues significantly in favor of [its] acceptance." *Blue Chip Stamps v. Manor Drug Stores,* 421 U.S. 723, 733 (1975).

The starting point for any inquiry regarding implied remedies is the intent of Congress in passing the statute in the first place. The Supreme Court's recent opinions, emphasizing that congressional intent must be the touchstone, have reaffirmed use of the test first articulated in *Cort v. Ash,* 422 U.S. 66 (1975), for ascertaining that intent.[22] There the Court outlined the following four-step analysis to guide efforts to determine legislative intent:

> First, is the plaintiff "one of the class for whose *especial* benefit the statute was enacted"—that is, does the statute create a federal right in favor of the plaintiff? Second, is there any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one? Third, is it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff? And finally, is the cause of action one traditionally relegated to state law, in an area basically the concern of the States, so that it would be inappropriate to infer a cause of action based solely on federal law?

Id. at 78 (citations omitted) (emphasis in original).

---

[22] Although one of the dissenters in *Cannon v. University of Chicago* would have discarded the *Cort* approach, *see* 441 U.S. 677, 742 (1979) (Powell, J., dissenting), the controversy has primarily revolved around how to apply *Cort,* not whether to apply it. *See Transamerica Mortgage Advisors, Inc. v. Lewis,* 444 U.S. 11, 23-24 (1979); *Touche Ross & Co. v. Redington,* 442 U.S. 560, 575-76 (1979); *Cannon,* 441 U.S. at 688.

Applying the *Cort* criteria, it is clear firstly that Wachovia is within the specific class to be protected by the statute. Section 10(b) proclaims as its purpose "the protection of investors." Secondly, as in other cases in which private remedies have been implied, a search of the legislative history yields little specific. Congress did not spend much time discussing 10(b), notwithstanding its clear place as a " 'catch-all clause to prevent manipulative devices.' " *Hochfelder,* 425 U.S. at 202 (quoting Thomas Corcoran, spokesperson for the drafters of the statute); *see Chiarella v. United States,* 445 U.S. 222, 226 (1980).

Such silence, however, is neither surprising nor determinative. *See Transamerica Mortgage Advisors, Inc. v. Lewis,* 444 U.S. 11, 18 (1979); *Cannon v. University of Chicago,* 441 U.S. 677, 694 (1979); *Blue Chip Stamps,* 421 U.S. at 737. If Congress had spoken plainly enough, the task would be simple. The quest, therefore, is not necessarily for evidence that Congress specifically intended to imply a private right of action, but rather for indications whether Congress meant to deny such a remedy. This was the thrust of *Transamerica.* There, the Court found legislative maneuverings that so reshaped earlier drafts of the statute at issue as to offer persuasive evidence that Congress wanted no implied remedies added to what the statute specifically provided.[23] No such legislative history disposes of the issue here.

Because the relevant legislative chronicles do not negative the existence of implied remedies, the third factor of *Cort* must be examined: whether a private remedy "is necessary or at least helpful to the accomplishment of the statutory purpose." *Cannon,* 441 U.S. at 703. We find more than the requisite link between the existence of an

[23] *See* text following note 26 *infra.*

implied cause of action and the broad purposes of the 1934 Act. A private right of action not only compensates the investors who are the beneficiaries of section 10(b) in general, but also affords a broad deterrent force against the fraud that the statute condemns. *See, e.g., Fratt v. Robinson,* 203 F.2d 627, 631 (9th Cir. 1953). And, as the SEC argues forcefully in its amicus position, a private remedy is a necessary supplement to administrative enforcement because the Commission cannot do the job alone. *See Blue Chip Stamps,* 421 U.S. at 730; *J.I. Case Co. v. Borak,* 377 U.S. 426, 432-33 (1964); *cf. Cannon,* 441 U.S. at 708 n.42.[24]

Application of the *Cort* criteria thus points in favor of appellants' right to pursue a cause of action here. Cross-appellants urge, however, that recent opinions of the Supreme Court have limited preexisting law in this are. We cannot read those cases to support a conclusion that a private remedy under section 10(b) no longer exists.

In *Cannon v. University of Chicago,* 441 U.S. 677 (1979), the Court held that there was a private right of action under Title IX of the Education Amendments of 1972, 20 U.S.C. § 1681 (1976), even though the statute itself specified no such cause of action. Among the two opinions recognizing an implied remedy and the two opinions in dissent, there was indeed reconciliation and reconsideration of earlier precedents. But the Court reiterated its

---

[24] The fourth factor outlined in *Cort*—whether the case involves matters traditionally of state or federal concern—is not as relevant as the first three in any inquiry into congressional intent. Nevertheless, that criterion is clearly satisfied here. As the court below found, appellants' complaint alleges a broad scheme to manipulate the national market for NSMC stock. Conduct with such national implications is exactly what Congress was interested in controlling when it provided for federal regulation of the securities markets in the 1934 Act. *See* § 2, 15 U.S.C. § 78b (1976).

adherence to earlier guidelines, in particular, the four-part test of *Cort v. Ash.* In fact, that was the core of the complaint voiced by Justice Powell in dissent, who advocated abandonment of the *Cort* approach. *See* 441 U.S. at 749.[25]

The second case cited as proof of this radical shift away from implied remedies is *Touche Ross & Co. v. Redington,* 442 U.S. 560 (1979). There the Court did reject urgings for an implied remedy for violations of section 17(a) of the Securities Act of 1934, 15 U.S.C. § 78q(a) (1976). The Court pointed out how frequently it was called upon to "decide whether a private remedy is implicit in a statute not expressly providing one." *Id.* at 562. But the Court did not announce that it was going out of the business.[26]

Most recently, in *Transamerica Mortgage Advisors, Inc. v. Lewis,* 444 U.S. 11 (1979), the Court refused to imply a cause of action under section 206 of the Investors Advisers Act of 1940, 15 U.S.C. § 80b-5 (1976), a statutory provision worded very similarly to Rule 10b-5. The Court relied there on two pieces of evidence weighing against implication of a private remedy. First, the Act nowhere provided for damage remedies, from which the Court inferred that Congress had been unwilling to impose any monetary liability in private suits under the Act. The 1933 and 1934 Acts do, of course, provide express damage remedies, and the Court in *Transamerica* specifically distinguished them.

---

[25] Even Justice Powell did not suggest that no private remedy should be implied under § 10(b); rather, he argued that implication of a cause of action under that section "reflects the unique history of Rule 10b-5" and does not "articulate any standards of general applicability." 441 U.S. at 738 (Powell, J., dissenting).

[26] For the Court in *Redington,* "the inquiry end[ed]" when (1) § 17(a) neither prohibited conduct nor granted private rights, but merely required that certain forms be filed, and (2) the legislative history was silent. 442 U.S. at 576. Here, of course, § 10(b) does specifically prohibit certain conduct.

See 444 U.S. at 20-21. Second, although early drafts of the Investors Advisers Act had given federal courts jurisdiction over "all suits in equity *and actions at law* brought to enforce any *liability or* duty" created by the statute, the final version appeared without the italicized phrases. The Court interpreted this omission as corroborating Congress' rejection of any civil liability. *See id.* at 21-22. In contrast, the 1934 Act's jurisdictional provision, 15 U.S.C. § 78aa (1976), is identical to the early version of the Investors Advisers Act quoted above.[27]

---

[27] In addition to those cases discussed above, the Supreme Court has recently failed to imply private rights of action in *Chrysler Corp. v. Brown*, 441 U.S. 281 (1979), and in *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1 (1977). Both are distinguishable from this case. In *Brown*, involving the Trade Secrets Act, 18 U.S.C. § 1905 (1976), the Court expressed reluctance to find an implied remedy in a criminal statute. And, "[m]ost importantly," the Court noted, a private right was not necessary to effectuate the purposes of the Act in that case because of the availability of review under § 10 of the Administrative Procedure Act, 5 U.S.C. § 702 (1976). 441 U.S. at 317-18.

In *Piper*, the Court rejected the contention of defeated tender offerors that they were entitled to a private remedy under § 14(e) of the 1934 Act, 15 U.S.C. § 78n(e) (1976), added by the Williams Act of 1968. The Court's decision was based on legislative history indicating that the sole purpose of the Williams Act was the protection of shareholders of target corporations. *See* 430 U.S. at 26-35. Moreover, the Court held, an implied remedy in favor of tender offerors might be inconsistent with that objective by awarding damages "to the very party whose activities Congress intended to curb." *Id.* at 39. Even if such damage awards might contribute indirectly to shareholder protection, the Court concluded that that objective could more directly be realized by "other, less drastic means more closely tailored to the precise congressional goal underlying the Williams Act." *Id.* at 40.

As made clear in our discussion accompanying notes 22-24 *supra*, the need for private remedies to supplement SEC enforcement of the 1934 Act and the absence of legislative history indicating congressional disapproval of such remedies distinguish the case before us and § 10(b) from the statutory provisions at issue in *Brown* and *Piper*.

It may be reasonable to infer from these recent pronouncements that the Court is not favorably inclined toward expanding the doctrine of implied remedies; it is unreasonable to imply, as cross-appellants seem to in their briefs, that all the implied remedies that have previously been established have now been swept away. In sum, we find that under the *Cort* analysis, section 10(b) continues to lend itself to private remedies, and that neither the spirit nor the letter of any Supreme Court opinion suggests otherwise.

B. *Application of Section 10(b) to Newly Issued Securities*

Cross-appellants argue that the entire 1934 Act, of which section 10(b) is a part, is inapplicable to this case because the Act was intended to regulate securities only after distribution. It is the 1933 Act, say cross-appellants, which was meant to cover newly issued securities. Such a rigidly compartmentalized analysis misses the clear intention of Congress and the overall purposes of the statutory scheme. Section 10(b) by its very terms applies to "any security," whether or not registered on a national exchange. The language was intended to be sweeping, and it has been so held. *See Affiliated Ute Citizens v. United States,* 406 U.S. 128, 151 (1972). In *SEC v. Capital Gains Research Bureau,* 375 U.S. 180, 195 (1963), the Court declared that Congress wanted securities legislation aimed at protecting against fraud to be construed "not technically and restrictively, but flexibly to effectuate its remedial purposes."

Cross-appellants advance the legislative history of the 1934 Act as supportive of their interpretation. Even if the language of section 10(b) were not so plain, its legislative history would offer cross-appellants little solace. That his-

tory corroborates Congress' intent, as noted above, that 10(b) act as a "catch-all clause to prevent manipulative devices." In fact, earlier drafts of the section limited its applicability to securities listed on a national exchange, but that restriction was removed in conference. *See* 1 A. BROMBERG, SECURITIES LAW: FRAUD § 2.2(320) (1977).

The broad scope of section 10(b) has been widely recognized, and the section has been applied to newly issued securities and to those sold in private placements. *See, e.g., Superintendent of Insurance v. Bankers Life & Casualty Co.*, 404 U.S. 6, 12 (1971) ("[W]e read § 10(b) to mean that Congress meant to bar deceptive devices and contrivances in the purchase or sale of securities whether conducted in the original markets or face to face."); *Woolf v. S.D. Cohn & Co.*, 515 F.2d 591, 606-07 (5th Cir. 1975), *vacated on other grounds*, 426 U.S. 944 (1976), *on remand*, 546 F.2d 1252 (5th Cir.), *cert. denied*, 434 U.S. 831 (1977); *Leasco Data Processing Equipment Corp. v. Maxwell*, 468 F.2d 1326, 1336 (2d Cir. 1972); *Lawrence v. SEC*, 398 F.2d 276, 280 (1st Cir. 1968); *Hooper v. Mountain States Securities Corp.*, 282 F.2d 195, 201 (5th Cir. 1960), *cert. denied*, 365 U.S. 814 (1961); *Fratt v. Robinson*, 203 F.2d 627, 629-31 (9th Cir. 1953).

Moreover, overlap between the two statutes is neither "unusual nor unfortunate." *SEC v. National Securities, Inc.*, 393 U.S. 453, 468 (1969), *quoted in United States v. Naftalin*, 441 U.S. 768, 778 (1979). It is nowhere written that each pronouncement of Congress must be mutually exclusive of every other pronouncement. In the securities field, Congress has dealt with the problems of regulations many times—on both the cosmic and the specific levels. The 1933 and 1934 Acts are meant to be interrelated and interdependent components of a general scheme, and the

two should be read together. *See Ernst & Ernst v. Hochfelder,* 425 U.S. 185, 206 (1976). There is no conflict between them, and their overlap in no way diminishes the plain meaning of section 10(b).

C. *The Relevance of Express Remedies*

Cross-appellants' final contention is that section 10(b) may not give rise to an implied remedy because other specific sections of the 1933 and 1934 Acts provide pertinent express remedies. The argument smacks somewhat of a "Catch 22" arrangement because in each instance cross-appellants are at the ready to show that the express remedies are not really available to Wachovia. And the argument has been unavailing in previous cases for reasons that are applicable here.

The ancient maxim *"expressio unius est exclusio alterius"* is a dangerous road map with which to explore legislative intent. As we have pointed out above, the nature of the legislative process militates against each enactment's being self-contained and mutually exclusive of every other enactment. Even in the context of a single piece of legislation, the existence of an express remedy arising under one section does not preclude the need for an implied remedy in other situations under other sections of the act. Such rigid analysis, noted the Supreme Court, would be an "excursion into extrapolation of legislative intent [that is] entirely unilluminating." *Cort v. Ash,* 422 U.S. 66, 83 n.14 (1975).

It is true that the Supreme Court has expressed concern about implying private rights of action when express remedies have been created by statute, but that concern has been limited to cases in which the express remedies would be nullified if additional remedies were implied. *See*

Touche Ross & Co. v. Redington, 442 U.S. 560, 574 (1979); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 208-11 (1976); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 736 (1975).[28] Such circumvention can hardly be an issue here, where the express remedies are totally different from the remedy implied under section 10(b), and where the express remedies are meant to treat different problems and to be applied in different situations.[29]

Section 11 of the 1933 Act,[30] for example, imposes civil liability for filing a false registration statement. Under

---

[28] *Cf. Greater Iowa Corp. v. McLendon*, 378 F.2d 783, 790 (8th Cir. 1967); *McFarland v. Memorex Corp.*, 493 F. Supp. 631, 653 (N.D. Cal. 1980); *Gunter v. Hutcheson*, 433 F. Supp. 42, 46-47 (N.D. Ga. 1977); *Dorfman v. First Boston Corp.*, 336 F. Supp. 1089, 1093-96 (E.D. Pa. 1972) (all holding that implied remedy under § 17(a) of the 1933 Act would circumvent limitations on express remedies provided by § 11 and § 12(2) of that Act).

[29] The Supreme Court has never decided whether the existence of express remedies precludes implication of a private right of action, and it specifically left the issue open in *Hochfelder*, 425 U.S. at 211 n.31, and in *Blue Chip Stamps*, 421 U.S. at 752 n.15. Dicta in *Redington* expressing reluctance to create an additional remedy when express remedies are already provided is not controlling in this case. In *Redington*, while the Court declined to decide the issue, *see* 442 U.S. at 574, it did note the existence of legislative history supporting a finding that the express remedies were intended to be exclusive. *See id.* at 573 & n.15. No such evidence exists here.

[30] In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security (unless it is proved that at the time of such acquisition he knew of such untruth or omission) may, either at law or in equity, in any court of competent jurisdiction, sue—

(1) every person who signed the registration statement;

(2) every person who was a director of (or person performing similar functions) or partner in the issuer

that provision, a defendant may be held liable even for negligent misstatements. Because of its broader liability, section 11's reach is limited by restrictions on the class of plaintiffs to whom its remedy is available and by a short and strict statute of limitations. To no one's surprise, the remedy is unavailable to Wachovia on both counts: no registration statement was filed, and the suit was brought well beyond the time allowed under section 11.

Nothing in the remedy expressly provided by section 11 is inconsistent with an implied right of action under section 10(b). Under 10(b), negligence is not enough—one is liable only for fraud. The higher burden of proof under section 10(b) is clearly a trade-off for the limitations on

---

at the time of the filing of the part of the registration statement with respect to which his liability is asserted;

(3) every person who, with his consent, is named in the registration statement as being or about to become a director, person performing similar functions, or partner;

(4) every accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him, who has with his consent been named as having prepared or certified any part of the registration statement, or as having prepared or certified any report or valuation which is used in connection with the registration statement, with respect to the statement in such registration statement, report, or valuation, which purports to have been prepared or certified by him;

(5) every underwriter with respect to such security.

If such person acquired the security after the issuer has made generally available to its security holders an earning statement covering a period of at least twelve months beginning after the effective date of the registration statement, then the right of recovery under this subsection shall be conditioned on proof that such person acquired the security relying upon such untrue statement in the registration statement or relying upon the registration statement and not knowing of such omission, but such reliance may be established without proof of the reading of the registration statement by such person.

Section 11(a), 15 U.S.C. § 77k(a) (1976).

section 11 claims, and it accounts in part for the fact that there are two separate sections dealing with related problems. *See Fischman v. Raytheon Mfg. Co.*, 188 F.2d 783, 786-87 (2d Cir. 1951); *Beecher v. Able*, 435 F. Supp. 397, 412 (S.D.N.Y. 1977). *See also Globus v. Law Research Service, Inc.*, 418 F.2d 1276, 1284 (2d Cir. 1969), *cert. denied*, 397 U.S. 913 (1970) (same argument applied when implying remedy under section 17(a) of the 1933 Act). Moreover, according to the view urged by cross-appellants, section 10(b) would serve no useful function because fraud is included within the broad proscription of section 11. Indeed, if no remedies may be implied under 10(b), investors defrauded in a purchase of unregistered securities are left less protected than investors suffering losses as the result of typographical errors in a registration statement.

For the same reasons, implying a remedy under section 10(b) creates no danger of circumvention of section 12(2) of the 1933 Act,[31] which deals with false prospectuses and

---

[31] Any person who—

. . . .

(2) offers or sells a security (whether or not exempted by the provisions of section 77c of this title other than paragraph (2) of subsection (a) of said section), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for

oral communications. The cause of action expressly provided by that section is available in the event of negligent misstatements, and again the more stringent fraud requirement of section 10(b) serves as a trade-off for section 12(2)'s short statute of limitations and apparent restriction of defendants to sellers of securities. *See Wachovia Bank & Trust Co. v. National Student Marketing Corp.*, 461 F. Supp. 999, 1006 (D.D.C. 1978). *See also In re New York City Municipal Securities Litigation*, MDL No. 314 M 21-22, slip op. at 16 & n.20 (S.D.N.Y. Jan. 25, 1980) (using similar analysis to approve section 10(b) suit by purchasers of municipal securities foreclosed from using express remedy of section 12(2), which exempts government securities).

Finally, cross-appellants point to section 18 of the 1934 Act[32] as providing an express remedy that precludes im-

---

such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

Section 12(2), 15 U.S.C. § 77*l*(2) (1976).

[32] Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this chapter or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 78*o* of this title, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading. A person seeking to enforce such liability may sue at law or in equity in any court of competent jurisdiction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant.

Section 18(a), 15 U.S.C. § 78r(a) (1976).

plication of a cause of action under section 10(b). Section 18 makes any person filing a "false or misleading" statement with the SEC liable for damages caused by reliance on that statement. Cross-appellants' contention was recently considered and rejected by the Second Circuit in *Ross v. A.H. Robins Co.*, 607 F.2d 545 (2d Cir. 1979), *cert. denied*, 100 S. Ct. 2175 (1980). The court there discussed various differences between the two sections which militate against regarding them as mutually exclusive.

First, section 10(b) by its very terms has a much broader reach than does section 18. The latter, noted the Second Circuit, has "the narrow and particularized objective of encouraging use of and reliance upon records filed with the S.E.C." *Ross*, 607 F.2d at 556. Section 18 therefore requires that plaintiffs prove actual reliance on particular filed statements, whereas section 10(b) presumes reliance if the omission is material or if the misstatement affects the price of the stock.

Second, section 10(b) imposes a more stringent burden of proof on plaintiffs—proof of actual fraud. Under section 18, a plaintiff need only show that a filed document contains a material omission or misstatement and that he relied on that document. The defendant then has the onus of establishing his good faith and lack of knowledge of the falsity. This distinction is noteworthy because, as the court noted in *Ross*, "the ultimate outcome of the litigation may hinge upon who bears the burden of establishing the defendant's state of mind." 607 F.2d at 556.

In addition to pointing out the differences between the express remedy of section 18 and an implied remedy under section 10(b), the Second Circuit also reasoned that a holding that the section 18 remedy is exclusive would be incongruous. Whether a misstatement occurs in a filed or

unfiled document has no bearing on the damage resulting from an investor's reliance on that document and therefore should not be considered significant. Moreover, if section 18's remedy is deemed exclusive, corporate managers will have an incentive to file misleading documents with the SEC in order to limit their liability to those few who can prove actual reliance on the documents. The very purpose of section 18—encouraging reliance on filed records—would be substantially frustrated.

We find *Ross* persuasive support for our holding that a cause of action may be implied under section 10(b), irrespective of the availability of the express remedies provided by other sections of the securities laws. By approving an implied remedy under section 10(b), we do not pave the way for circumvention of the limitations on the express remedies. The absence of similar restrictions in section 10(b) suits is counterbalanced by that section's stricter burden of proof. The various remedies are aimed at righting different wrongs, and no one of them should therefore be considered exclusive.[33]

Even if we were inclined to hold that the express remedies were intended to be exclusive, they should only preclude implied causes of action in those cases in which they truly constitute "remedies." Where, as here, those express remedies are not available to a plaintiff or do not

---

[33] Other courts have agreed that the remedies of the two Acts are cumulative and that plaintiffs have a choice in the event of overlap. *See Shaefer v. First Nat'l Bank*, 509 F.2d 1287, 1292 (7th Cir. 1975), *cert. denied*, 425 U.S. 943 (1976); *Wolf v. Frank*, 477 F.2d 467, 475 (5th Cir.), *cert. denied*, 414 U.S. 975 (1973); *Rekant v. Desser*, 425 F.2d 872, 882 (5th Cir. 1970); *Jordan Bldg. Corp. v. Doyle, O'Connor & Co.*, 401 F.2d 47, 51 (7th Cir. 1968); *Matheson v. Armbrust*, 284 F.2d 670, 674 (9th Cir. 1960). *But see McFarland v. Memorex Corp.*, 493 F. Supp. 631, 655 (N.D. Cal. 1980).

adequately dispose of his claim, an implied remedy is appropriate.[34]

In this case, relief was not available to Wachovia under any of the aforementioned provisions. The scope of section 11 of the 1933 Act is restricted to false registration statements, and the transaction here, because it did not involve a public offering, was not subject to the registration requirement. *See* section 4(2) of the 1933 Act, 15 U.S.C. § 77d(2) (1976). Cross-appellants may not be sued under section 12(2) of the 1933 Act, which limits potential defendants to sellers. *See Wachovia,* 461 F. Supp. at 1006; *Collins v. Signetics Corp.,* 605 F.2d 110, 113 (3d Cir. 1979); *DeMarco v. Edens,* 390 F.2d 836, 841 n.3 (2d Cir. 1968). Finally, plaintiffs have not claimed reliance on any documents filed with the SEC and thus may not bring suit under section 18 of the 1934 Act. Moreover, they have alleged materially false statements which were never contained in a filed document and which are thus exempt from section 18 liability. *See Wachovia,* 461 F. Supp. at 1006.[35]

In contrast to the inapplicability of the express remedies provided by the 1933 and 1934 Acts, an action under sec-

---

[34] Even those few district courts holding that plaintiffs are limited to the express remedy of § 18 have done so only with respect to particular documents filed with the SEC. *See, e.g., McKee v. Federal's Inc.,* [Current] FED. SEC. L. REP. (CCH) ¶ 96,958 (E.D. Mich. 1979); *Pearlstein v. Justice Mortgage Investors,* [Current] FED. SEC. L. REP. (CCH) ¶ 96,760 (N.D. Tex. 1978); *Berman v. Richford Indus., Inc.,* [1978] FED. SEC. L. REP. (CCH) ¶ 96,518 (S.D.N.Y. 1978); *Kulchok v. Government Employees Ins. Co.,* [1977-1978] FED. SEC. L. REP. (CCH) ¶ 96,002 (D.D.C. 1977).

[35] Cross-appellants also mention the express private right of action provided by § 15 of the 1933 Act, 15 U.S.C. § 77*o* (1976). That section imposes secondary liability on the controlling persons of NSMC, but no suit could have been maintained under § 15 against cross-appellants, who are not controlling persons. *See Safeway Portland Employees' Federal Credit Union v. C.H. Wagner & Co.,* 501 F.2d 1120, 1124 & n.17 (9th Cir. 1974).

tion 10(b) is particularly appropriate here. That provision is concerned with the type of fraud alleged by plaintiffs—"a complex market manipulation rather than individual misstatements or omissions." *Wachovia,* 461 F. Supp. at 1007; *see Blackie v. Barrack,* 524 F.2d 891, 903 n.19, 907 (9th Cir. 1975), *cert. denied,* 429 U.S. 816 (1976). Appellants should, therefore, be able to maintain a cause of action under section 10(b), the only true relief available to them. We hold that appellants may pursue their claims under that section, regardless of whether an alternative remedy is available to them under some other section of the 1933 or 1934 Act.

It has become fashionable to challenge the existence of any implied remedies, as evidenced by the ever-increasing frequency with which the question has been presented to the Supreme Court and to other courts. *See Redington,* 442 U.S. at 562. We find nothing in the opinions of either the Supreme Court or of the other courts of appeals to warrant the suggestion that implied remedies no longer exist. Most recently, the Court of Appeals for the Second Circuit found a private remedy implied by the Commodity Exchange Act, 7 U.S.C. §§ 1-24 (1976). *See Leist v. Simplot,* 49 U.S.L.W. 2056 (July 22, 1980). That case arose out of the notorious Maine potato futures default. The defendants urged the court to deny a private remedy because Congress had amended the Commodity Exchange Act in 1974 and had failed to include an express private remedy in the sections pertinent to the case. The court pointed out:

> The existence of an implied right of action under the Act as it stood in 1974 was repeatedly called to the attention of, and implicitly approved by, Congress. When a principle has become settled through court

> decisions, there is no occasion for Congress to speak unless it wishes a change.

Id.

As we noted above, the securities laws have been addressed by Congress on numerous occasions since 1934, most recently in 1975. Obviously, if Congress had wished to disapprove the judicial implication of a private remedy under section 10(b), it had an opportunity to do so. The silence is significant. *Cf. Power Reactor Development Co. v. International Union of Electrical, Radio & Machine Workers,* 367 U.S. 396, 409 (1961).

The court in *Leist* also addressed the argument that the Supreme Court has changed the law of implied remedies. After reviewing the Court's recent opinions, which we have discussed above, the Second Circuit rejected the argument, saying

> [t]he effect of these decisions is simply to emphasize that the ultimate touchstone is congressional intent and not judicial notions of what would constitute wise policy.

49 U.S.L.W. at 2057. We read those cases alike. Just as it would be lawmaking for the courts to decide what good policy is in the first instance, so too the courts ought not retract for policy reasons a longstanding doctrine of legislative interpretation, especially one impliedly approved by Congress. It is the prerogative of Congress, presumed to be aware of how its enactments have been treated, to sound the call for a new direction.

IV. Conclusion

It is more than a decade since the collapse of NSMC stock, and long past time that appellants be given an opportunity to pursue the substance of their claims and, if appropriate, to recover for losses incurred as NSMC shareholders and alleged victims of securities fraud. We reverse the holding of the court below that it is the two-year statute of limitations for the District of Columbia's blue sky law that applies here and the holding that the doctrine of equitable tolling is unavailable to appellants. Accordingly, we find that this action is not time-barred under the District's three-year limitations period for general fraud claims.

We hold further that appellants may rely on a remedy implicit under section 10(b) of the 1934 Act, irrespective of the possibility of overlap between that implied cause of action and express remedies provided by other sections of the securities laws. Section 10(b) is peculiarly appropriate to the allegations of fraud made by appellants, and we find nothing in the legislative history of the securities laws or in recent Supreme Court opinions inconsistent with an implied right of action under section 10(b).

Reversed and remanded.

Opinion of United States District Court

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF COLUMBIA

M.D.L. No. 105

Civil Action No. 166-73

WACHOVIA BANK AND TRUST CO., N.A., *et al.*,

Plaintiffs,

v.

NATIONAL STUDENT MARKETING CORP., *et al.*,

Defendants.

APPEARANCES

JUAN A. DEL REAL, Esquire
RICHARD M. PHILLIPS, Esquire
HILL, CHRISTOPHER AND PHILLIPS, P.C.
Washington, D. C. 20036

Attorneys for Plaintiffs

MILTON V. FREEMAN, Esquire
THOMAS D. NURMI, Esquire
ROBERT H. WINTER, Esquire
ARNOLD & PORTER
Washington, D. C. 20036

Attorneys for Defendants White & Case and Marion Jay Epley, III

WILLIAM E. HEGARTY, Esquire
MATHIAS E. MONE, Esquire
HARVEY J. GOLUBOCK, Esquire
JOSEPH W. MUCCIA, Esquire
CAHILL GORDON & REINDEL
New York, New York 10005

Attorneys for Defendants Peat, Marwick, Mitchell & Co., Anthony M. Natelli and Joseph Scansaroli

Before

BARRINGTON D. PARKER
United States District Judge

Decided: November 20, 1978

MEMORANDUM OPINION

Barrington D. Parker, District Judge:

In this private federal securities laws litigation, filed by the Wachovia Bank and Trust Company and other plaintiffs[1] (the Wachovia plaintiffs), two questions are presented for the Court's resolution. First, do the plaintiffs have implied causes of action under § 17(a) of the Securities Act of 1933 (1933 Act)[2] and §§ 10(b), 13(a) and 14(a) of the Securities Exchange Act of 1934 (1934 Act)?[3] Second, is this private action, brought under these statutory sections,

---

[1] This is one of several private law suits growing out of the National Student Marketing Corporation stock fraud scheme. M.D.L. No. 105. The plaintiffs in this proceeding are Wachovia Bank and Trust Co., First Wisconsin Trust Co., The Dreyfus Offshore Trust, and the National Fire Insurance Company of Hartford. *See* note 7 *infra*.

[2] 15 U.S.C. § 77q(a).

[3] 15 U.S.C. §§ 78j(b), 78m(a) and 78n(a).

barred by the applicable statute of limitations and, if so, is there an independent cause of action based on common law fraud, breach of fiduciary duty and legal malpractice?

These issues have been raised by the law firm of White & Case, Marion J. Epley, a partner, and the accounting firm of Peat, Marwick, Mitchell & Co. (Peat Marwick).[4] The defendants have moved for judgment on the pleadings under Rule 12(c), Federal Rules of Civil Procedure, or alternatively to dismiss the complaint with prejudice under Rule 12(b)(6).

The Court has considered the various memoranda, affidavits and exhibits filed as well as the oral argument of counsel. For the reasons set forth herein the Court finds that plaintiffs have stated a private cause of action under § 17(a) of the 1933 Act and § 10(b) of the 1934 Act and, therefore, defendants' motion for judgment on the pleadings on the issue of implied causes of action is denied. However, the Court agrees with the defendants on the statute of limitations issue and concludes that the federal claims asserted by plaintiffs are time-barred and the remaining claims must be dismissed for lack of pendent jurisdiction.

Introduction

In late 1969 when the economic fortunes of the National Student Marketing Corporation (NSMC) were most favorable and the reports on its financial operations extremely optimistic, the Wachovia plaintiffs purchased at a private placement nearly five million dollars worth of that corporation's stock. The terms of the purchase were governed by two contracts between the parties, dated December 17, 1969. White & Case, acting as NSMC's counsel, drafted

[4] The defendants also include Anthony M. Natelli and Joseph Scansaroli, members of Peat Marwick.

a Common Stock Purchase Agreement and issued a legal opinion to plaintiffs. Peat Marwick, the independent auditor of NSMC, certified the annual financial statements and played a role in preparation of interim financial reports and documents filed with the Securities and Exchange Commission (SEC).

In February of 1970, almost immediately following the Wachovia transaction, NSMC's fortunes suffered a sharp reversal and the stock's market price dropped markedly.[5] Shortly thereafter, in early 1970, two civil actions arising out of the collapse were filed in the Southern District of New York federal court. *Garber v. Randell,* (March 2, 1970); *Lipsig v. National Student Marketing Corp.,* (May 15, 1970) (naming Peat Marwick as defendant). In early 1972, a third action was filed in the Southern District, *Natale v. National Student Marketing Corp.,* (February 18, 1972) (naming White & Case as defendant).[6] Also, on March 19, 1970, a civil complaint was filed in the Southern District of Texas federal court. *Stuckey v. National Student Marketing Corp.,* (March 19, 1970). While White & Case and Peat Marwick were not parties in either *Garber* or *Stuckey,* the complaints outlined the alleged fraudulent scheme and financial manipulation that underlie the Wach-

---

[5] The low bid price fell from 69½ on December 17, 1969, to 26 on February 17, 1970 (after giving effect to a two-for-one stock split). National Quotation Bureau Report, Dec. 1, 1976, at 16, 18.

[6] Marion J. Epley, III, was first named as a defendant in the Consolidated, Amended and Supplemental Complaint, *Garber v. Randell,* No. 70-835 (S.D.N.Y. June 2, 1972).

Taken together, the New York class action filings were complaints brought on behalf of all purchasers of NSMC stock who made their purchases between April 1, 1968, and February 17, 1972, and therefore included the Wachovia group as "asserted" class members. On November 29, 1972, following formal class certification and notice, the Wachovia plaintiffs officially "opted out" of the class.

ovia complaint. A complaint was also filed in October 1971 in the Southern District of Ohio, *Monroe v. Peat, Marwick, Mitchell & Co.*, alleging that the accountants aided and abetted others in misrepresenting Student Marketing's financial condition.

In February 1972, the SEC filed an enforcement and injunctive action against the major participants in the corporate acquisition and merger of National Student Marketing and Interstate National Corporation.[7] White & Case and Peat Marwick, among others, were named as defendants in that proceeding.

Despite this turn of events, more than three years elapsed after their December 1969 purchase before the Wachovia plaintiffs sought relief. On January 29, 1973, their original complaint was filed seeking damages from NSMC, several of its officers and employees; Peat Marwick, the partner in charge of the Washington, D.C., office, Anthony M. Natelli; and the auditor, Joseph Scansaroli. The complaint charged those named defendants with a conspiracy to defraud and violations of applicable federal securities laws in connection with plaintiffs' purchase of NSMC common stock in 1969.[8] The complaint did not include any common law counts.

On January 27, 1973, two days before this suit was filed, the Wachovia plaintiffs and the attorney-defendants entered into a letter agreement that the statute of limitations would be tolled for two years from that date as to them.[9]

---

[7] *SEC v. National Student Marketing Corp.*, 457 F.Supp. 682 (D.D.C. 1978).

[8] The plaintiffs have since settled and dismissed their claims against NSMC and various named defendants.

[9] The tolling letter, dated January 27, 1973, provides that:

> White & Case and Mr. Epley are agreeable to the tolling of the statute of limitations for a period of two years from the date of this letter as to claims of [the plaintiffs] against White

By its terms, however, no claims could be asserted which were then barred by any applicable provision of law.

It was not until May 28, 1975, that the Wachovia plaintiffs amended their original complaint to include White & Case and Epley as defendants. The amended complaint charges those attorneys with various securities laws violations in addition to common law fraud, breach of fiduciary duty and legal malpractice.

In addition to the motions of the attorney and accountant defendants addressed in this opinion, the Wachovia plaintiffs seek to amend the original complaint, largely to raise common law fraud claims against Peat Marwick and the other remaining original defendants. Also before the Court is a motion of the defendant Roger O. Walther, a principal executive officer of NSMC and a major participant in its operations. He seeks to amend his answer to raise the statute of limitations defense.

THE IMPLIED CAUSES OF ACTION ISSUE

In seeking dismissal of all claims asserted under § 17(a) of the 1933 Act and §§ 10(b) or 14(a) of the 1934 Act,[10] the

---

& Case and Mr. Epley arising out of the purchase of NSMC securities . . . in December, 1969. . . .

. . . .

In any such litigation or suit brought by [the plaintiffs] after termination or expiration of the tolling period, if White & Case and Mr. Epley plead the statute of limitations as to any claims by [the plaintiffs], it is further understood that any period during which the statute of limitations is tolled pursuant to this letter shall be excluded from the computation of the running of the limitation period. This letter shall not apply to and shall not revive any claims which [the plaintiffs], as of the date of this letter, are already barred from asserting by any applicable provisions of law.

[10] Plaintiffs' claim under § 13(a) of the 1934 Act has been abandoned.

defendants contend in substance that since certain provisions of the securities laws expressly provide private remedies for the conduct alleged here, the Wachovia plaintiffs cannot bypass the substantive and procedural limitations of those provisions by basing their claims for relief on judicially implied causes of action under the above-cited provisions. Resort to the express remedies is now time-barred and thus dismissal of the present implied claims would effectively foreclose any recovery under the federal securities laws. Plaintiffs strenuously object that their allegations encompass conduct which is not covered by the express provisions and which clearly falls within the recognized scope of implied causes of action.

The Court concludes that plaintiffs have stated a claim under § 17(a) of the 1933 Act and § 10(b) of the 1934 Act. However, even assuming an implied action would be appropriate under § 14(a) of the 1934 Act, they have failed to state a claim under that provision.

Initially, it should be noted that defendants do not contest the implication of a private remedy under all circumstances, and for good reason, since an implied right of action has been recognized repeatedly under § 10(b), *see, e.g., Ernst & Ernst v. Hochfelder,* 425 U.S. 185, 196, 96 S.Ct. 1375, 47 L. Ed. 2d 668 (1976); *Blue Chip Stamps v. Manor Drug Stores,* 421 U.C. 723, 730, 95 S.Ct. 1917, 44 L. Ed. 2d 539 (1975). With less frequency and certitude, such an action has also been sanctioned under § 17(a), *see, e.g., Daniel v. International Brotherhood of Teamsters,* 561 F.2d 1223, 1244-45 (7th Cir. 1977), *cert. granted,* 434 U.S. 1061, 98 S.Ct. 1232, 55 L.Ed. 2d 761 (1978); *Forrestal Village, Inc. v. Graham,* 179 U.S. App. D.C. 225, 551 F.2d 411, 413 (1977); *but see Shull v. Dain, Kalman & Quail, Inc.,* 561 F.2d 152, 159 (8th Cir. 1977), *cert. denied,* 434 U.S. 1086,

98 S.Ct. 1281, 55 L.Ed. 2d 792 (1978). Rather, the defendants urge that where an express remedy covers the conduct alleged, judicial implication of a cause of action is not necessary to effectuate the goals of the securities laws. *See Santa Fe Industries, Inc. v. Green,* 430 U.S. 462, 477, 97 S.Ct. 1292, 51 L.Ed. 2d 480 (1977); *Piper v. Chris-Craft Industries, Inc.,* 430 U.S. 1, 41, 97 S.Ct. 926, 51 L.Ed. 2d 124 (1977). Thus, they do not appear to argue that implied actions under § 17(a) or § 10(b) are inapplicable to the conduct alleged, but only that such implied remedies are unnecessary under the facts and circumstances here presented since express remedies were available if the plaintiffs had chosen to use them.

Defendants contend that § 18(a) of the 1934 Act[11] and § 12(2) of the 1933 Act[12] provide remedies for the mis-

---

[11] Section 18(a), 15 U.S.C. § 78r, provides:

> Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this chapter or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 78o of this title, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading. A person seeking to enforce such liability may sue at law or in equity in any court of competent jurisdiction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant.

[12] Section 12(2), 15 U.S.C. § 77l, provides:

> Any person who—
>
> . . . .
>
> (2) offers or sells a security . . . by the use of any means or instruments of transportation or communication in interstate

statements and omissions alleged by plaintiffs. Specifically, they assert that most, if not all, of the materially false and misleading statements are substantially contained in documents filed with the SEC and are thus subject to the remedy provided by § 18(a). Insofar as certain statements may not be contained in such filed documents, they urge that § 12(2) provides an adequate remedy.

This Court is not persuaded that these express remedies suffice to effectuate congressional intent, as indicated by the securities laws, to proscribe the type of fraudulent conduct alleged here. With limited exceptions, plaintiffs do not allege reliance upon documents filed with the SEC and, contrary to the position of defendants, such reliance is essential to recovery under § 18(a). *Heit v. Weitzen,* 402 F.2d 909, 916 (2d Cir. 1968), *cert. denied,* 395 U.S. 903, 89 S.Ct. 1740, 23 L.Ed.2d 217 (1969); *Gross v. Diversified Mortgage Investors,* 438 F. Supp. 190, 195 (S.D.N.Y. 1977). The fact that statements similar to those alleged by plaintiffs were also contained in documents filed with the SEC is insufficient; absent reliance upon the filing of the state-

---

commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission, shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

ments with the Commission, § 18(a) is inapplicable.[13] In addition, plaintiffs have alleged materially false statements which were never contained in a document filed with the SEC and thus are clearly exempt from § 18(a) liability.

Defendants respond that the remedy for such nonfiled statements rests with § 12(2). That provision, however, contains a number of restrictions, based in large part on the fact that it reaches even negligent misstatements and omissions, and is not directed solely at the intentional fraud alleged here. It appears doubtful that Congress intended victims of intentional fraud to be limited to the negligence remedy provided by § 12(2). Moreover, there is some question whether the section applies to the present defendants since they were not "sellers" of the securities in question. *See e.g., In re Equity Funding Corp. of America Securities Litigation,* 416 F. Supp. 161, 181 (C.D. Cal. 1976). While such a restriction is appropriate in a negligence context, it clearly is unwarranted here where the participants are charged with intentional fraud.

In short, it appears that neither § 18(a) nor § 12(2) provides the plaintiffs with adequate remedies. If the Court were to recognize defendants' solution, the plaintiffs would be relegated to state courts to pursue their claims based on common law fraud. Such a suggestion needs little discussion. The gravamen of plaintiffs' complaint is that defendants participated in a scheme to manipulate the national market for NSMC stock through the broad dissemination of materially false and misleading state-

---

[13] It is unclear whether reliance must be on the actual document filed with the SEC, or whether reliance on a copy of such document would suffice. The latter seems to be the more reasonable position since it is the knowledge that it has been filed with the Commission that justifies reliance on the document.

ments concerning NSMC. Such conduct is clearly a matter of federal, not state, concern. *See* 15 U.S.C. § 78b.[14]

Since this is not a case where the allegations in the complaint fall entirely within the scope of express provisions of the securities laws,[15] and since the allegations primarily

---

[14] Section 78b, 15 U.S.C., provides:

> transactions in securities as commonly conducted upon securities exchanges and over-the-counter markets are affected with a national public interest which makes it necessary to provide for regulation . . . in order to protect interstate commerce, the national credit, . . . and to insure the maintenance of fair and honest markets in such transactions:
>
> . . . .
>
> (3) Frequently the prices of securities on such exchanges and markets are susceptible to manipulation and control, and the dissemination of such prices gives rise to excessive speculation. . . .

[15] An implied cause of action should be available even where the alleged misconduct also falls completely within the confines of an express remedy. "The fact that there may well be some overlap is neither unusual nor unfortunate," *SEC v. National Securities, Inc.*, 393 U.S. 453, 468, 89 S.Ct. 564, 573, 21 L.Ed.2d 668 (1969), especially since recent developments have properly restricted such implied remedies to the scope authorized by specific statutory provisions. *See TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 96 S.Ct. 2126, 48 L.Ed.2d 757 (1976) (materiality); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 96 S.Ct. 1375, 47 L.Ed.2d 668 (1976) (scienter); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 95 S.Ct. 1917, 44 L.Ed.2d 539 (1975) (purchaser/seller). Moreover, to conclude that express and implied causes of action should not overlap would require a case-by-case determination of the applicability of implied remedies under the particular factual situation presented. Such a procedure, especially in a pretrial stage when the factual bases for the various claims have not been developed, would significantly burden an already complex area of the law.

But see Kulchock v. Government Employees Insurance Co., [Transfer Binder '77-'78 Decisions] Fed. Sec. L. Rep. (CCH) ¶ 96,002 (D.D.C. 1977) (complaint dismissed on ground that there is no implied cause of action for misstatements in documents filed with the SEC because § 18 of the 1934 Act provides express remedy

concern a complex market manipulation rather than individual misstatements or omissions, *see Blackie v. Barrack,* 524 F.2d 891, 907 (9th Cir. 1975), *cert. denied,* 429 U.S. 816, 97 S.Ct. 57, 50 L.Ed.2d 75 (1976), the Court concludes that plaintiffs have stated a claim under § 10(b) of the 1934 Act and § 17(a) of the 1933 Act.[16]

A different conclusion is reached with respect to plaintiffs' asserted cause of action under § 14(a) of the 1934 Act. To support such a claim, plaintiffs must allege an injury to their corporate suffrage rights or an injury resulting from a corporate transaction whose approval was obtained by a misleading proxy statement. *In re Penn Central Securities Litigation,* 347 F. Supp. 1327, 1342 (E.D. Pa. 1972), *aff'd,* 494 F.2d 528 (3rd Cir. 1974). In an attempt to meet the second part of the test, the Wachovia plaintiffs allege that the stock they purchased was authorized on the basis of the misleading NSMC proxy material concerning the Interstate transaction. The Court does not read the test so broadly. Plaintiffs' injury did not result from the authorization of the stock, but from their later purchase of it at an allegedly inflated price. To state a claim under the second part of the test, the alleged stock transaction must be part of the merger itself and not a subsequent transaction. Therefore, plaintiffs have failed to state a claim under § 14(a) and defendants' motion to dismiss claims

---

for same); appeal of this dismissal Order withdrawn in light of final judgment and settlement, C.A. No. 76-206 (D.D.C. July 28, 1978).

[16] Since defendants' motions are primarily directed to the distinction between express and implied remedies, the Court need not consider the relationship between the two implied causes of action.

Defendants make other minor arguments in support of their motions to dismiss, none of which have merit.

asserted under that provision must be granted. Of course, to the extent allegations contained in these claims are also applicable to the alleged manipulative scheme, they are properly brought under § 10(b) and § 17(a). *See* 347 F. Supp. at 1342.

THE STATUTE OF LIMITATIONS ISSUE

A. Motion of White & Case and Epley

The District of Columbia Securities Act, the so-called "blue sky law," includes a statute of limitations which in part provides that:

> No person may bring an action under this section after two years from the contract of sale . . . .[17]

Only recently our Circuit ruled that when a private action is brought under § 10(b) of the 1934 Act and § 17(a) of the 1933 Act, this two-year blue sky period is the applicable statute of limitations. *Forrestal Village, Inc. v. Graham,* 179 U.S. App. D.C. 225, 551 F.2d 411 (1977). Since the Wachovia plaintiffs allege violations of §§ 10(b) and 17(a), and their other claims concern securities fraud, *Forrestal Village* mandates application of the two-year statute of limitations.

The pending claims against the attorney-defendants were not filed until May 1975, though, by virtue of the tolling letter, it must be assumed that theses claims were filed on January 27, 1973.[18] Both of these dates are more than two years after the December 17, 1969, contracts of sale. The defendants accordingly urge that the securities laws

---

[17] D.C. Code § 2-2413(e) (1973).

[18] *See* p. 1004 and note 9.

claims are untimely filed under the blue sky law and should be dismissed with prejudice. Because plaintiffs' common law claims are allegedly dependent upon the time-barred securities claims, defendants contend that the Court should not exercise pendent jurisdiction over the state law claims.

Plaintiffs argue initially that *Forrestal Village* should not be applied retroactively and that they are entitled to the benefits of the D.C. three-year statute of limitations for common law fraud actions.[19] Citing the criteria of *Chevron Oil Co. v. Huson,* 404 U.S. 97, 106-07, 92 S.Ct. 349, 30 L.Ed.2d 296 (1971), they allege that *Forrestal Village* overrules the only precedent in the District and therefore creates a new principle of law which cannot fairly be applied retroactively.

The Court, in agreement with defendants, cannot accept this argument. Indeed, White & Case point out that prior law is by no means unequivocal, consisting largely of three unreported United States District Court cases, all of which barred actions under the three-year general fraud limitations period.[20] The *Forrestal Village* court did not announce a new general principle of law, but "join[ed] the majority of circuits" in applying a local blue sky law statute of limitations in securities fraud cases. 551 F.2d at 413. Lastly, this Court has already applied the decision retroactively. *Houlihan v. Anderson-Stokes,* 434 F. Supp. 1324 (D.D.C. 1977).

Having adopted the blue sky provision, the Court must next determine when the two-year period commenced to run. Plaintiffs' principal opposition to defendants' motion

---

[19] D.C. Code § 12-301(8) (1973).

[20] *See* Reply by Defendants White & Case and Marion J. Epley, III, to Plaintiffs' Memorandum in Opposition to Motion to Dismiss the Complaint, August 26, 1977, at 18-22.

to dismiss is that the federal common law tolling doctrine is applicable and held the limitations period in abeyance until such time as the alleged fraud was or should have been discovered. They identify the relevant date as February 3, 1972, when the SEC filed its injunction action before this Court.[21] Only then, they contend, was it that "[t]he first hint of any participation by White & Case in the massive NSMC stock fraud surfaced . . . ." [22]

The federal tolling doctrine appears in *Bailey v. Glover*, where the Supreme Court announced that:

> the decided weight of authority is in favor of the proposition that where the party injured by the fraud *remains in ignorance of it without any fault or want of diligence or care on his part*, the bar of the statute does not begin to run until the fraud is discovered, though there be no special circumstances or efforts on the part of the party committing the fraud to conceal it from the knowledge of the other party.

88 U.S. (21 Wall.) 342, 348, 22 L.Ed. 636 (1875) (emphasis added). Where federal securities laws violations are alleged, as here, this time-honored doctrine has been recognized to mean that the statute of limitations cannot be said to run until a plaintiff, in the exercise of reasonable diligence, discovered or should have discovered the fraudulent activity underlying his cause of action.[23] The law is also

---

[21] *See* note 7 *supra*.

[22] Plaintiffs' Memorandum in Opposition to Motion by Defendants White & Case and Marion J. Epley, III, July 29, 1977, at 2.

[23] *Cook v. Avien, Inc.*, 573 F.2d 685, 694-95 (1st Cir. 1978); *Arneil v. Ramsey*, 550 F.2d 774, 780-01 (2d Cir. 1977); *Newman v. Prior*, 518 F.2d 97, 100 (4th Cir. 1975); *Tomera v. Galt*, 511 F.2d 504, 509 (7th Cir. 1975); *Hudak v. Economic Research*

clear that the statutory period will not await a plaintiff's leisurely discovery of the full details of the fraudulent scheme, but begins to run when plaintiff possesses sufficient information, which in the exercise of due diligence, warrants further inquiry.[24]

White & Case and Epley do not contend that the Wachovia plaintiffs had actual knowledge of their participation in the fraudulent scheme. Instead, they allege that the facts were such that plaintiffs, four large sophisticated institutional investors, should have formulated some suspicion against the law firm shortly after the private placement in 1969. Defendants label the following uncontroverted occurrences, established and known to the public in early 1970, as "code blue" alert notices of fraud:

> a. The precipitous decline of NSMC stock within sixty days after the plaintiffs' purchase, from 69½ on December 17, 1969, to 26 on February 17, 1970;[25]

Analysts, Inc., 499 F.2d 996, 1001-02 (5th Cir. 1974), *cert. denied*, 419 U.S. 1122, 95 S.Ct. 805, 42 L.Ed.2d 821 (1975); *Vanderboom v. Sexton*, 422 F.2d 1233, 1240 (8th Cir. 1970), *cert. denied*, 400 U.S. 852, 91 S.Ct. 47, 27 L.Ed.2d 90 (1970); *Janigan* v. *Taylor*, 344 F.2d 781, 784 (1st Cir. 1965), *cert. denied*, 382 U.S. 879, 86 S.Ct. 163, 15 L.Ed.2d 120 (1965); *Long v. Abbott Mortgage Corp.*, 459 F.Supp. 108 (D. Conn. 1978).

[24] *Cook v. Avien, Inc.*, *supra* note 23, at 696; *Klein v. Bower*, 421 F.2d 338, 343 (2d Cir. 1970).

[25] *See* p. 2 and note 5 *supra* and affidavit of Thomas D. Nurmi, filed October 26, 1977.

See also Hupp v. Gray, 500 F.2d 993, 996-97 (7th Cir. 1974) (dramatic fall in market price from $47 per share to $17.50 per share, rather than the $75 predicted to the purchaser, sufficient to put wholly unsophisticated investor on notice that "something was amiss"); *Robertson v. Seidman & Seidman*, [Current] Fed.Sec.L. Rep. (CCH) ¶ 96,420 (S.D.N.Y. May 3, 1978) (85% decline in value of stock over less than a year, among other signs, should have led plaintiff to suspect fraud). *See also Cook v. Avien, Inc.*, *supra* note 23, at 696.

b. The loss, ranging from 1.2 to 1.7 million dollars, reported in early 1970 by NSMC for the quarter ended November 30, 1969;[26] and

c. News articles reporting NSMC financial difficulties in *Barron's* (December 12, 1969) and *The Wall Street Journal* (February 17, 1970).

In addition to the above, it is established that in early 1970, key officials of two plaintiffs, The Dreyfus Offshore Trust (general counsel and vice president) and First Wisconsin Trust Company (investment analyst), commenced investigation and contemplated suit.[27]

The Court agrees that these facts, coupled with the several lawsuits filed in 1970, provided a clearly marked trail which, if pursued with diligence, would have led the plaintiffs to the fraud of the NSMC officials and to the attorney-defendants and their involvement in the stock sale. A statute of limitations does not become operative when a

---

[26] This loss was reported in the national press, including the February 17, 1970, *Wall Street Journal*.

[27] Lawrence M. Greene, general counsel and vice president of Dreyfus, began investigating in January 1970. When questioned concerning the *Barron's* article of December 12, 1969, his deposition at p. 118 reads:

> Q. Is it your understanding that upon your review of the Barron's article in January of 1970 that any subsequent investigations you made with respect to National Student Marketing were in contemplation of litigation?
>
> A. I was greatly concerned when I read the article . . . . , and, in fact, *I was rather upset about it and I therefore began to investigate the situation more deeply.* Whatever I did following that in connection with looking into the facts is *all part and parcel of my turning the matter over to our counsel for litigation.* (emphasis added).

Robert G. Steffel, an investment analyst, testified that First Wisconsin Trust was contemplating suit in late 1970 or early 1971.

plaintiff discovers all aspects of a fraudulent scheme, but rather from the time when a clue to the facts, if pursued diligently, would lead to an uncovering of the general fraudulent scheme. *Berry Petroleum Co. v. Adams & Peck*, 518 F.2d 402, 410 (2d Cir. 1975); *Klein v. Bower*, 421 F.2d 338, 343 (2d Cir. 1970).

This situation is virtually indistinguishable from that in the recent § 10(b) case of *Robertson v. Seidman & Seidman*, [Current] Fed. Sec. L. Rep. (CCH) ¶ 96,420 (S.D.N.Y. May 3, 1978). In that proceeding an investor asserted that the defendant-accountants certified false and misleading financial statements in a stock sale. The district court granted summary judgment and dismissed the complaint as time-barred, holding that the investor should have discovered the fraud more than two years before suit was filed. The investor relied upon the federal tolling doctrine, claiming ignorance of the accountants' role until a later time when the SEC announced proceedings against them. The court found that the investor should have discovered the fraud far earlier, because the evidence showed that in the intervening period: the stock dropped markedly in value; he had suspected fraud and had discussed it with his broker; and was aware of a class action suit arising out of the same stock offering, charging price inflation through dissemination of false and misleading information. While that class complaint did not specifically name the accountants, the court found that "the plaintiff should at least have been on notice that further inquiry into the fraudulent practices surrounding . . . the public offering would be prudent," *Robertson* at 93,518, and there were public facts available indicating the accountants' role.

There is no difference between *Robertson* and this action except for the involvement of accountants rather than

attorneys. That of course is of no consequence. The Wachovia plaintiffs knew that White & Case had drafted the Stock Purchase Agreement as well as the legal opinion to secure their purchase. Their blanket claim that before the SEC injunctive action was filed in 1972 they had no reason to suspect this "reputable and prestigious" law firm of any unlawful role in a stock sale is rejected. As responsible money managers and investors, they had a duty to pursue every aspect of the transaction, including the role of the legal counsel in such a suspect sale. Their experience and their access to highly specialized personnel and consultants imposed an obligation of reasonable diligence commensurate with their sophistication and standing in the financial community.

> Whatever is notice enough to excite attention and put the party on his guard and call for inquiry, is notice of everything to which such inquiry might have led. When a person has sufficient information to lead him to a fact, he shall be deemed conversant of it. . . . The presumption is that if the party affected by any fraudulent transaction or management might, with ordinary care and attention, have seasonably detected it, he seasonably had actual knowledge of it.

Wood v. Carpenter, 101 U.S. 135, 141, 25 L.Ed. 807 (1879).

Plaintiffs argue that the question as to when they had knowledge of White & Case's fraud and the issue of reasonable care as grounds for tolling the statute are disputed factual issues and cannot be disposed of without a trial. The Court disagrees. *See Jones v. Rogers Memorial Hospital,* 143 U.S. App. D.C. 51, 53, 442 F.2d 773, 775 n.2 (1971). The National Student Marketing matters were consolidated for pretrial discovery and have been pending for more than

five years. All parties in this proceeding have conducted expensive, time consuming and exhaustive discovery. The papers, exhibits and argument on these motions have been especially thorough and, in this Court's opinion, if there are any undisclosed facts at this stage, their relevancy and materiality are minimal.

Taken as a whole, the record is more than sufficient to show that plaintiffs should have investigated the attorney-defendants' potential role in the suspicious sale and should have known of the fraud within the two-year statute of limitations, running immediately after the sale. Plaintiffs' complaint as to White & Case and Epley is untimely filed and the motion of these defendants to dismiss must be granted. With dismissal of the federal claims at this time, the pendent state common law claims fall as well. *United Mine Workers v. Gibbs,* 383 U.S. 715, 726, 86 S.Ct. 1130, 16 L.Ed.2d 218 (1966); *Robertson v. Seidman & Seidman, supra,* at 93,519; *Hupp v. Gray,* 500 F.2d 993, 997 (7th Cir. 1974).

B. *Motion of Peat Marwick, Natelli and Scansaroli*

In seeking dismissal, the accountant-defendants adopt in large measure the White & Case and Epley argument that *Forrestal Village* controls and that, in this private action under §§ 17(a) and 10(b) of the federal securities laws, the applicable statute of limitations is the two-year provision of the District of Columbia blue sky law. To counter the federal tolling doctrine urged by the Wachovia investors, they point to the several private actions filed in the New York federal courts, particularly the *Lipsig* class action of May 15, 1970, the first to name Peat Marwick as a defendant. The accountant-defendants also argue that those law suits, together with other events and developments widely publicized in the financial community, were

yellow caution lights, all ignored by Wachovia. Since the complaint under consideration was not brought until January 29, 1973, the federal tolling doctrine does not protect the plaintiffs.

The plaintiffs on the other hand allege and urge that filing of the several New York class actions, of which they were asserted members, tolled the running of the limitations period. The *Lipsig, Garber* and *Natale* complaints were filed on behalf of NSMC shareholders who made their stock purchases between April 1968 and February 1972, and did indeed include plaintiffs as purported members. These actions were consolidated in April 1972 and later transferred by the Judicial Panel on Multidistrict Litigation to this Court for pretrial proceedings. The New York actions were certified as class actions and, during October 1973, notice of class action determination was sent to the various class members including the Wachovia plaintiffs.

In January 1973, however, the Wachovia plaintiffs had filed the present complaint naming Peat Marwick, Natelli and Scansaroli among the defendants. In justification for their course of action they asserted that their status as institutional purchasers made their complaint dissimilar to the earlier class actions. On November 29, 1973, they "opted out" to pursue their independent claims.

Peat Marwick argues that the Wachovia plaintiffs should have filed an action within two years of the 1969 purchase and that the January 1973 complaint is therefore time-barred. The accountant-defendants contend that the statute of limitations was not tolled by the various class actions, because by opting out, the plaintiffs forfeited any benefits accruing to the class members. As members in the earlier filed class action proceedings the Wachovia plaintiffs could

not exclude themselves from the class and then file law suits which otherwise would be time-barred.

The class action tolling doctrine is best illustrated in *American Pipe & Construction Co. v. Utah*, 414 U.S. 538, 94 S.Ct. 756, 38 L.Ed.2d 713 (1974), where the Supreme Court held that filing of a class action complaint tolls the running of the statute of limitations for all purported class members who timely seek intervention after the lower court has found the asserted class too small to certify. According to the Court, a contrary rule allowing participation only by those potential class members who had earlier filed motions to intervene would deprive class actions of the efficiency and economy of litigation which they are designed to promote. This rule is not inconsistent with the functional operation of a statute of limitations, since the policies of ensuring fairness to defendants and of barring plaintiffs who have slept on their rights are satisfied when a named plaintiff "notifies the defendants not only of the substantive claims being brought against them, but also of the number and generic identities of the potential plaintiffs who may participate in the judgment." 414 U.S. at 554-55, 94 S.Ct. at 767.

In light of these policy considerations, this Circuit has called for a "broad, functional" reading of *American Pipe*.[28] *McCarthy v. Kleindienst*, 562 F.2d 1269, 1274 (D.C. Cir. 1977). The court there extended the *American Pipe* tolling doctrine to a case where a motion for class certification had been denied not because of size but on grounds of untimeli-

---

[28] *See also United Airlines, Inc. v. McDonald*, 432 U.S. 385, 97 S.Ct. 2464, 53 L.Ed.2d 423 (1977) (potential class members could intervene after final judgment for the purpose of appealing the denial of class certification, even though the limitations period had run).

ness and nonpredominance of common questions. The court found that a motion to intervene brought by 266 asserted class members four years after the events at issue, but one day after denial of class certification, was timely, because there was no evidence of manipulative behavior by the plaintiffs and the defendants had received "sufficient notice of the contours of potential claims to toll the running of the statute of limitations." 562 F.2d at 1275. *See also United Airlines, Inc. v. McDonald,* 432 U.S. 385, 97 S.Ct. 2464, 53 L.Ed.2d 423 (1977).

The *American Pipe* line of cases concerns the propriety of intervention following denial of class certification. Here, there has been certification of a class which includes the Wachovia plaintiffs. Before that certification decision, plaintiffs filed a separate action. Following certification, they opted out of the class rather than pursuing class relief. The broad issue here, therefore, is whether the policy considerations of *American Pipe* operate to toll the limitations period for all purported class members until certification is decided.

The Court finds that, under the circumstances presented here, the class action tolling doctrine does not protect the Wachovia complaint brought against the accountant-defendants. Preliminarily, the doctrine cannot operate against defendants Natelli and Scansaroli. Since they were not named in the original New York actions, they cannot fairly be charged with the notice requisite for class action tolling. Notice considerations also mean that the consolidated amended complaint naming them, filed on June 2, 1972, does not relate back for tolling purposes. *Arneil v. Ramsey,* 550 F.2d 774, 782 n. 10 (2d Cir. 1977).[29]

---

[29] The amendment came more than two years after the *Lipsig* action naming Peat Marwick. Therefore, even if the latter suit

Insofar as Peat Marwick is concerned, plaintiffs base their opposition to the motion largely on a footnote in a Supreme Court class action decision following *American Pipe*. In *Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 94 S.Ct. 2140, 40 L.Ed.2d 732 (1974), a case concerning notice to potential class members, the Court referred to *American Pipe* as establishing that

> commencement of a class action tolls the applicable statute of limitations as to all members of the class. 417 U.S. at 176 n.13, 94 S.Ct. at 2152.

While at least one court has found that this dictum "appears to have . . . eliminated" the general tolling question,[30] this Court is not so persuaded. There is precedent supporting an interpretation opposite to plaintiffs' in the Second Circuit. In *Arneil v. Ramsey, supra,* that court refused to toll the running of the statute of limitations for a separate action brought by two plaintiffs who were not asserted members of a class action as originally filed. *See also Stull v. Bayard,* 561 F.2d 429, 433 (2d Cir. 1977), *cert. denied,* 434 U.S. 1035, 98 S.Ct. 769, 54 L.Ed.2d 783 (1978).

For the Court to find otherwise, that the class action filings tolled the limitations period for plaintiffs' separate suit, would sanction duplicative suits and violate the policies behind *American Pipe*. Even assuming that this action

---

should have put plaintiffs on notice that individual accountants at Peat Marwick were involved in the fraud, the federal tolling doctrine cannot be added to the class action tolling doctrine to protect the suit against Natelli and Scansaroli.

[30] *Agostine v. Sidcon Corp.*, 69 F.R.D. 437, 448 n.13 (E.D. Pa. 1975) (Truth in Lending case). *See also McAlpine v. AAMCO Automatic Transmissions, Inc.*, 1977-1 Trade Cases ¶ 61,359 (E.D. Mich. 1977) (antitrust case—court found dicta "highly persuasive" and tolled the statute of limitations for damage purposes).

and the original class actions raise identical issues, the filing of a class action should not cause Peat Marwick to be responsible for meeting separate independent actions by class members after their statute of limitations has run. If different issues are raised, there is even less reason to credit Peat Marwick with notice.

The Court also finds it noteworthy that the plaintiffs filed this action before class certification had been decided. If, following certification, they had determined that the class action strategy would not protect their rights and had then promptly filed a separate action, their arguments might be more persuasive. By filing their action before a certification decision, opting out of the class after certification, and then claiming the benefits of tolling, they appear to have been manipulating the tolling doctrine and other class action procedures. While the Court is aware that *American Pipe* had not been decided as of January 29, 1973, when plaintiffs filed this action, their delay is not justifiable in light of the traditional purposes of a statute of limitations.

Since the Wachovia plaintiffs are not protected by the class action tolling doctrine, their complaint against Peat Marwick was not timely filed and must be dismissed. In light of this disposition, it is not necessary for the Court to address Peat Marwick's contention that the instant action does not involve the same issues raised in the New York actions.

Other Motions

a. In light of the Court's dismissal of the Wachovia plaintiffs' complaint against the accountant-defendants, the motion of the plaintiffs to amend the complaint to add common law fraud claims against Peat Marwick, Natelli and

Scansaroli is denied. The Court would not exercise pendent jurisdiction over such state claims if the amendment were allowed. *See* p. 12 *supra*.

The motion to amend will also be denied insofar as plaintiffs seek to amend the caption to reflect the parties who have not settled, given that various cross-claims are pending and such a technical change is not necessary. The motion will be granted, at this time, only insofar as plaintiffs seek to delete references to § 13(a) of the 1934 Act under the Count I heading.

b. The Court finds that defendant Walther's motion to amend his answer to raise a statute of limitations defense is appropriate. In light of the pleadings that have been filed on this issue, the plaintiffs will not be prejudiced by the amendment.

c. The motion of the Wachovia plaintiffs to compel White & Case and Epley to produce documents, memoranda allegedly prepared for counsel, does not bear on the factual issues involved in these motions and will be denied as moot.

ORDERED accordingly.

Entered: November 20, 1978

BARRINGTON D. PARKER
United States District Judge

Order Denying Rehearing

UNITED STATES COURT OF APPEALS

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 79-1595

September Term, 1980

Argued 12-13-79

WACHOVIA BANK AND TRUST CO., N.A. (as Trustee and Agent for various trust accounts), *et al.*

Appellants

v.

NATIONAL STUDENT MARKETING CORPORATION, *et al.*,

And consolidated cases

Before:

ROBINSON and MIKVA, *Circuit Judges*;

FLANNERY, *Judge, United States District Court for the District of Columbia*

ORDER

This matter is before the Court for consideration of the petitions for rehearing of Peat, Marwick, Mitchell & Co., Anthony M. Natelli and Joseph Scansaroli, White and Case and Marion Jay Epley, III, Joy Walther, Donald A. Fergusson and Robert A. Fergusson, and the motion of Cortes W. Randell for leave to file petition for rehearing out of time, it is

Order Denying Rehearing

ORDERED by the Court that the motion of Cortes W. Randall for leave to file out of time is denied, and, it is

FURTHER ORDERED by the Court that all of the aforesaid petitions for rehearing are denied.

Per Curiam

FOR THE COURT:

George A. Fisher, *Clerk*

By: /s/ ROBERT A. BONNER
Robert A. Bonner
Chief Deputy Clerk

FILED MARCH 4, 1981

GEORGE A. FISHER, *Clerk*

Order Denying Rehearing *En Banc*

UNITED STATES COURT OF APPEALS

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 79-1595

September Term, 1980

Civil Action No. 166-73

Argued 12-13-79

WACHOVIA BANK AND TRUST CO., N.A. (as Trustee and Agent for various trust accounts), *et al.*

Appellants

v.

NATIONAL STUDENT MARKETING CORPORATION, *et al.*,

And consolidated cases

Before:

McGOWAN, *Chief Judge;*

WRIGHT, TAMM, ROBINSON, MacKINNON, ROBB, WILKEY, WALD, MIKVA, EDWARDS and GINSBURG, *Circuit Judges*

ORDER

This matter is before the Court for consideration of the suggestions for rehearing *en banc* of Peat, Marwick, Mitchell & Co., Anthony M. Natelli and Joseph Scansaroli, White and Case and Marion Jay Epley, III, Joy Walther, Donald A. Fergusson and Robert A. Fergusson. These suggestions

have been circulated to the full Court. A majority of the judges have not voted in favor of rehearing this matter *en banc*. On consideration of the foregoing, it is

ORDERED by the Court *en banc*, that all of the aforesaid suggestions are denied.

Circuit Judges MacKinnon and Robb would rehear these cases *en banc*.

Circuit Judge Wright did not participate in the foregoing order.

Per Curiam

FOR THE COURT:

George A. Fisher, *Clerk*

By: /s/ ROBERT A. BONNER
Robert A. Bonner
Chief Deputy Clerk

FILED MARCH 4, 1981

GEORGE A. FISHER, *Clerk*

Securities Act of 1933

§ 5, 15 U.S.C. § 77e (1976)

§ 77e. Prohibitions relating to interstate commerce and the mails

(a) Sale or delivery after sale of unregistered securities

Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.

(b) Necessity of prospectus meeting requirements of section 77j of this title.

It shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or transmit any prospectus relating to any security with respect to which a registration statement has been filed under this subchapter, unless such prospectus meets the requirements of section 77j of this title; or

(2) to carry or cause to be carried through the mails or in interstate commerce any such security for the

purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of subsection (a) of section 77j of this title.

(c) Necessity of filing registration statement

It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 77h of this title.

* * *

§ 11, 15 U.S.C. § 77k (1976)

§ 77k. Civil Liabilities on account of false registration statement

(a) Persons possessing cause of action; persons liable

In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security (unless it is proved that at the time of such acquisition he knew of such untruth or omission) may, either at law or in equity, in any court of competent jurisdiction, sue—

(1) every person who signed the registration statement;

(2) every person who was a director of (or person performing similar functions) or partner in the issuer at the time of the filing of the part of the registration statement with respect to which his liability is asserted;

(3) every person who, with his consent, is named in the registration statement as being or about to become a director, person performing similar functions, or partner;

(4) every accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him, who has with his consent been named as having prepared or certified any part of the registration statement, or as having prepared or certified any report or valuation which is used in connection with the registration statement, with respect to the statement in such registration statement, report, or valuation, which purports to have been prepared or certified by him;

(5) every underwriter with respect to such security.

If such person acquired the security after the issuer has made generally available to its security holders an earning statement covering a period of at least twelve months beginning after the effective date of the registration statement, then the right of recovery under this subsection shall be conditioned on proof that such person acquired the security relying upon such untrue statement in the registration statement or relying upon the registration statement and not knowing of such omission, but such reliance may be established without proof of the reading of the registration statement by such person.

(b) Persons exempt from liability upon proof of issues

Notwithstanding the provisions of subsection (a) of this section no person, other than the issuer, shall be liable as provided therein who shall sustain the burden of proof—

(1) that before the effective date of the part of the registration statement with respect to which his liability is asserted (A) he had resigned from or had taken such steps as are permitted by law to resign from, or ceased or refused to act in, every office, capacity, or relationship in which he was described in the registration statement as acting or agreeing to act, and (B) he had advised the Commission and the issuer in writing that he had taken such action and that he would not be responsible for such part of the registration statement; or

(2) that if such part of the registration statement became effective without his knowledge, upon becoming aware of such fact he forthwith acted and advised the Commission, in accordance with paragraph (1) of this subsection, and, in addition, gave reasonable public notice that such part of the registration statement had become effective without his knowledge; or

(3) that (A) as regards any part of the registration statement not purporting to be made on the authority of an expert, and not purporting to be a copy of or extract from a report or valuation of an expert, and not purporting to be made on the authority of a public official document or statement, he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state

a material fact required to be stated therein or necessary to make the statements therein not misleading; and (B) as regards any part of the registration statement purporting to be made upon his authority as an expert or purporting to be a copy of or extract from a report or valuation of himself as an expert, (i) he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or (ii) such part of the registration statement did not fairly represent his statement as an expert or was not a fair copy of or extract from his report or valuation as an expert; and (C) as regards any part of the registration statement purporting to be made on the authority of an expert (other than himself) or purporting to be a copy of or extract from a report or valuation of an expert (other than himself), he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue or that there was an omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or that such part of the registration statement did not fairly represent the statement of the expert or was not a fair copy of or extract from the report or valuation of the expert; and (D) as regards any part of the registration statement purporting to be a statement made by an official person or purporting to be a copy of or extract from a public official document,

he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue, or that there was an omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or that such part of the registration statement did not fairly represent the statement made by the official person or was not a fair copy of or extract from the public official document.

(c) Standard of reasonableness

In determining, for the purpose of paragraph (3) of subsection (b) of this section, what constitutes reasonable investigation and reasonable ground for relief, the standard of reasonableness shall be that required of a prudent man in the management of his own property.

(d) Effective date of registration statement with regard to underwriters

If any person becomes an underwriter with respect to the security after the part of the registration statement with respect to which his liability is asserted has become effective, then for the purposes of paragraph (3) of subsection (b) of this section such part of the registration statement shall be considered as having become effective with respect to such person as of the time when he became an underwriter.

(e) Measure of damages; undertaking for payment of costs

The suit authorized under subsection (a) of this section may be to recover such damages as shall represent the dif-

ference between the amount paid for the security (not exceeding the price at which the security was offered to the public) and (1) the value thereof as of the time such suit was brought, or (2) the price at which such security shall have been disposed of in the market before suit, or (3) the price at which such security shall have been disposed of after suit but before judgment if such damages shall be less than the damages representing the difference between the amount paid for the security (not exceeding the price at which the security was offered to the public) and the value thereof as of the time such suit was brought: *Provided*, That if the defendant proves that any portion or all of such damages represents other than the depreciation in value of such security resulting from such part of the registration statement, with respect to which his liability is asserted, not being true or omitting to state a material fact required to be stated therein or necessary to make the statements therein not misleading, such portion of or all such damages shall not be recoverable. In no event shall any underwriter (unless such underwriter shall have knowingly received from the issuer for acting as an underwriter some benefit, directly or indirectly, in which all other underwriters similarly situated did not share in proportion to their respective interests in the underwriting) be liable in any suit or as a consequence of suits authorized under subsection (a) of this section for damages in excess of the total price at which the securities underwritten by him and distributed to the public were offered to the public. In any suit under this or any other section of this subchapter the court may, in its discretion, require an undertaking for the payment of the costs of such suit, including reasonable attorney's fees, and if judgment shall be rendered against a party litigant, upon

the motion of the other party litigant, such costs may be assessed in favor of such party litigant (whether or not such undertaking has been required) if the court believes the suit or the defense to have been without merit, in an amount sufficient to reimburse him for the reasonable expenses incurred by him, in connection with such suit, such costs to be taxed in the manner usually provided for taxing of costs in the court in which the suit was heard.

(f) Joint and several liability

All or any one or more of the persons specified in subsection (a) of this section shall be jointly and severally liable, and every person who becomes liable to make any payment under this section may recover contribution as in cases of contract from any person who, if sued separately, would have been liable to make the same payment, unless the person who has become liable was, and the other was not, guilty of fraudulent misrepresentation.

(g) Offering price to public as maximum amount recoverable

In no case shall the amount recoverable under this section exceed the price at which the security was offered to the public.

§ 12, 15 U.S.C. § 77*l* (1976)

§ 77*l*. Civil liabilities arising in connection with prospectuses and communications

Any person who—

(1) offers or sells a security in violation of section 77e of this title, or

(2) offers or sells a security (whether or not exempted by the provisions of section 77c of this title, other than paragraph (2) of subsection (a) of said section), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

§ 13, 15 U.S.C. § 77m (1976)

§ 77m. Limitation of actions

No action shall be maintained to enforce any liability created under section 77k or 77*l*(2) of this title unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence, or, if the action is to enforce a liability created under section 77*l*(1) of this title, unless brought within one year after the violation upon which it is based. In no event

shall any such action be brought to enforce a liability created under section 77k or 77*l*(1) of this title more than three years after the security was bona fide offered to the public, or under section 77*l*(2) of this title more than three years after the sale.

• • •

§ 16, 15 U.S.C. § 77p (1976)

§ 77p. Additional remedies

The rights and remedies provided by this subchapter shall be in addition to any and all other rights and remedies that may exist at law or in equity.

§ 17, 15 U.S.C. § 77q (1976)

§ 77q. Fraudulent interstate transactions

(a) Use of interstate commerce for purpose of fraud or deceit

It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

(b) Use of interstate commerce for purposes of offering for sale

It shall be unlawful for any person, by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, to publish, give publicity to, or circulate any notice, circular, advertisement, newspaper, article, letter, investment service, or communication which, though not purporting to offer a security for sale, describes such security for a consideration received or to be received, directly or indirectly, from an issuer, underwriter, or dealer, without fully disclosing the receipt, whether past or prospective, of such consideration and the amount thereof.

(c) Exemption of section 77c not applicable to this section

The exemptions provided in section 77c of this title shall not apply to the provisions of this section.

* * *

Securities Exchange Act of 1934

§ 9, 15 U.S.C. § 78i (1976)

§ 78i. Manipulation of security prices

(a) Transactions relating to purchase or sale of security

It shall be unlawful for any person, directly or indirectly, by the use of the mails or any means or instrumentality of interstate commerce, or of any facility of any national securities exchange, or for any member of a national securities exchange—

(1) For the purpose of creating a false or misleading appearance of active trading in any security registered on a national securities exchange, or a false or misleading appearance with respect to the market for any such security, (A) to effect any transaction in such security which involves no change in the beneficial ownership thereof, or (B) to enter an order or orders for the purchase of such security with the knowledge that an order or orders of substantially the same size, at substantially the same time, and at substantially the same price, for the sale of any such security, has been or will be entered by or for the same or different parties, or (C) to enter any order or orders for the sale of any such security with the knowledge that an order or orders of substantially the same size, at substantially the same time, and at substantially the same price, for the purchase of such security, has been or will be entered by or for the same or different parties.

(2) To effect, alone or with one or more other persons, a series of transactions in any security registered on a national securities exchange creating actual or apparent active trading in such security or raising

or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others.

(3) If a dealer or broker, or other person selling or offering for sale or purchasing or offering to puchase the security, to induce the purchase or sale of any security registered on a national securities exchange by the circulation or dissemination in the ordinary course of business of information to the effect that the price of any such security will or is likely to rise or fall because of market operations of any one or more persons conducted for the purpose of raising or depressing the prices of such security.

(4) If a dealer or broker, or other person selling or offering for sale or purchasing or offering to puchase the security, to make, regarding any security registered on a national securities exchange, for the purpose of inducing the purchase or sale of such security, any statement which was at the time and in the light of the circumstances under which it was made, false or misleading with respect to any material fact, and which he knew or had reasonable ground to believe was so false or misleading.

(5) For a consideration, received directly or indirectly from a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to induce the purchase or sale of any security registered on a national securities exchange by the circulation or dissemination of information to the effect that the price of any such security will or is likely to rise or fall because of the market

operations of any one or more persons conducted for the purpose of raising or depressing the price of such security.

(6) To effect either alone or with one or more other persons any series of transactions for the purchase and/or sale of any security registered on a national securities exchange for the purpose of pegging, fixing, or stabilizing the price of such security in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(b) Transactions relating to puts, calls, straddles, or options

It shall be unlawful for any person to effect, by use of any facility of a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors—

(1) any transaction in connection with any security whereby any party to such transaction acquires any put, call, straddle, or other option or privilege of buying the security from or selling the security to another without being bound to do so; or

(2) any transaction in connection with any security with relation to which he has, directly or indirectly, any interest in any such put, call, straddle, option, or privilege; or

(3) any transaction in any security for the account of any person who he has reason to believe has, and who actually has, directly or indirectly, any interest

in any such put, call, straddle, option, or privilege with relation to such security.

(c) Endorsement or guarantee of puts, calls, straddles, or options

It shall be unlawful for any member of a national securities exchange directly or indirectly to endorse or guarantee the performance of any put, call, straddle, option, or privilege in relation to any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(d) Registered warrant, right, or convertible security not included in "put", "call", "straddle", or "option"

The terms "put", "call", "straddle", "option", or "privilege" as used in this section shall not include any registered warrant, right, or convertible security.

(e) Persons liable; suits at law or in equity

Any person who wilfully participates in any act or transaction in violation of subsections (a), (b), or (c) of this section, shall be liable to any person who shall purchase or sell any security at a price which was affected by such act or transaction, and the person so injured may sue in law or in equity in any court of competent jurisdiction to recover the damages sustained as a result of any such act or transaction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant.

Every person who becomes liable to make any payment under this subsection may recover contribution as in cases of contract from any person who, if joined in the original suit, would have been liable to make the same payment. No action shall be maintained to enforce any liability created under this section, unless brought within one year after the discovery of the facts constituting the violation and within three years after such violation.

§ 10, 15 U.S.C. § 78j (1976)

§ 78j. Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

(a) To effect a short sale, or to use or employ any stop-loss order in connection with the purchase or sale, of any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

• • •

Securities Exchange Act of 1934

§ 18, 15 U.S.C. § 78r (1976)

§ 78r. Liability for misleading statements

(a) Persons liable; persons entitled to recover; defense of good faith; suit at law or in equity; costs, etc.

Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this chapter or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 78o of this title, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading. A person seeking to enforce such liability may use at law or in equity in any court of competent jurisdiction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant.

(b) Contribution

Every person who becomes liable to make payment under this section may recover contribution as in cases of contract from any person who, if joined in the original suit, would have been liable to make the same payment.

(c) Period of limitations

No action shall be maintained to enforce any liability created under this section unless brought within one year after the discovery of the facts constituting the cause of action and within three years after such cause of action accrued.

• • •

§ 28(a), 15 U.S.C. § 78bb(a) (1976)

§ 78bb. Effect existing law

(a) The rights and remedies provided by this chapter shall be in addition to any and all other rights and remedies that may exist at law or in equity; but no person permitted to maintain a suit for damages under the provisions of this chapter shall recover, through satisfaction of judgment in one or more actions, a total amount in excess of his actual damages on account of the act complained of. Nothing in this chapter shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this chapter or the rules and regulations thereunder.

No. 80-1684

Office-Supreme Court, U.S.
FILED
MAY 15 1981
ALEXANDER L. STEVAS, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

PEAT, MARWICK, MITCHELL & Co.,
ANTHONY M. NATELLI and JOSEPH SCANSAROLI,
Petitioners,

v.

WACHOVIA BANK AND TRUST CO., N.A., MELLON BANK, N.A., FIRST WISCONSIN TRUST CO., THE DREYFUS OFFSHORE TRUST, N.V., and NATIONAL FIRE INSURANCE CO. OF HARTFORD,
Respondents.

SUPPLEMENTAL BRIEF IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

WILLIAM E. HEGARTY
80 Pine Street
New York, New York 10005
(212) 825-0100
Counsel of Record

VICTOR M. EARLE, III
345 Park Avenue
New York, New York 10022
Attorneys for Petitioners

Of Counsel:

MATHIAS E. MONE
JOSEPH W. MUCCIA
CAHILL GORDON & REINDEL
80 Pine Street
New York, New York 10005

May 1981

TABLE OF CONTENTS

PAGE

1. The "implied" remedy 1

2. Retroactivity 5

CONCLUSION 6

TABLE OF AUTHORITIES

Cases:

Blue Chip Stamps v. *Manor Drug Stores*, 421 U.S. 723 (1975) 2

California v. *Sierra Club*, 49 U.S.L.W. 4441 (U.S. April 28, 1981) 4, 5

Chevron Oil Co. v. *Huson*, 404 U.S. 97 (1971) 5

City of Milwaukee v. *Illinois*, 49 U.S.L.W. 4445 (U.S. April 28, 1981) 4, 5

Complete Auto Transit, Inc. v. *Reis*, 49 U.S.L.W. 4473 (U.S. May 4, 1981) 4

Ernst & Ernst v. *Hochfelder*, 425 U.S. 185 (1976) 2

Forrestal Village, Inc. v. *Graham*, 551 F.2d 411 (D.C. Cir. 1977) 5

Holzsager v. *The Valley Hospital*, No. 80-7839 (2d Cir. April 10, 1981) 5

Huddleston v. *Herman & MacLean*, 640 F.2d 534 (5th Cir. 1981) 1, 2, 3

Northwest Airlines, Inc. v. *Transport Workers Union*, 49 U.S.L.W. 4383 (U.S. April 20, 1981) 4

Santa Fe Industries, Inc. v. *Green*, 430 U.S. 462 (1977) 2

PAGE

Sharp v. *Coopers & Lybrand*, No. 80-2229 (3d Cir. April 28, 1981) 3

Touche Ross & Co. v. *Redington*, 442 U.S. 560 (1979) 2

Transamerica Mortgage Advisors, Inc. v. *Lewis*, 444 U.S. 11 (1979) 2

Universities Research Ass'n v. *Coutu*, 49 U.S.L.W. 4354 (U.S. April 6, 1981) 4, 5

Statutes:

Securities Act of 1933
§ 11, 15 U.S.C. § 77k (1976) 2
§ 12, 15 U.S.C. § 77l (1976) 2
§ 17, 15 U.S.C. § 77q (1976) 4

Securities Exchange Act of 1934
§ 10(b), 15 U.S.C. § 78j(b) (1976) ..... *passim*
§ 18, 15 U.S.C. § 78r (1976) 2

Rules:

Rule 22.6, Rules of the Supreme Court of the United States 1

No. 80-1684

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

PEAT, MARWICK, MITCHELL & Co.,
ANTHONY M. NATELLI and JOSEPH SCANSAROLI,

Petitioners,

v.

WACHOVIA BANK AND TRUST Co., N.A., MELLON BANK, N.A., FIRST WISCONSIN TRUST Co., THE DREYFUS OFFSHORE TRUST, N.V., and NATIONAL FIRE INSURANCE Co. OF HARTFORD,

Respondents.

SUPPLEMENTAL BRIEF IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

This supplemental brief is filed by PMM pursuant to Rule 22.6 of the Rules of the Court to call attention to decisions of courts of appeals and of the Court not available at the time PMM filed its petition for a writ of certiorari which bear upon the questions presented.

1. *The "implied" remedy.* The courts of appeals continue to disregard Congressional intent and to formulate conflicting rules concerning liability under § 10(b) of the 1934 Act. Recent decisions from the Third and Fifth Circuits, and the continuing massive federal litigation which they evidence, emphasize the reasons for granting the writ and deciding the first question at this time.

In *Huddleston* v. *Herman & MacLean,* 640 F.2d 534 (5th Cir. 1981), the Court of Appeals for the Fifth Circuit held

that a private cause of action may be implied under § 10(b) of the 1934 Act where the actions alleged "would also warrant a suit under Sections 11 and 12(2) of the 1933 Act. . . ." (640 F.2d at 541) The court observed that the issue had been posed and left open by this Court.

> "The apparent overlap in the applicability of the express liability provisions of the 1933 Act and the implied remedies raises the issue whether an implied cause of action is available when an express cause of action has been created, a question reserved by the Supreme Court in *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 752 n.15, 95 S.Ct. 1917, 1933 n.15, 44 L. Ed.2d 539, 559 n.15 (1975), and again left open in *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 211 n.31, 96 S.Ct. 1375, 1389 n.31, 47 L. Ed.2d 668, 687 n.31 (1976), in considering the relationship of Section 10(b) and Section 18 of the 1934 Act, 15 U.S.C. § 78r." (*Ibid.*)

The court said that this Court's decisions in *Blue Chip Stamps*, *Hochfelder*, *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462 (1977), *Touche Ross & Co.* v. *Redington*, 442 U.S. 560 (1979), and *Transamerica Mortgage Advisors, Inc.* v. *Lewis*, 444 U.S. 11 (1979), "give substance to the argument that no remedy should be implied for actions covered by express liability provisions of the statutes" (640 F.2d at 541-42 & n.6), but rejected that argument. The court did not once refer to Congressional intent, and said that it was "not being asked to create a new judicial remedy." (640 F.2d at 542)

The court in *Huddleston* went on to set out its view of the elements of a § 10(b) cause of action. In contrast to the decision of the court of appeals below that the § 10(b) remedy "presumes reliance if the omission is material or if the misstatement affects the price of the stock" (32a),

the court in *Huddleston* held "reliance is an issue in *all* Rule 10b-5 cases." (640 F.2d at 548) (emphasis in original) The court in *Huddleston* held that where as in this case against PMM the complaint "involve[s] alleged misstatements and omissions" in "published" financial statements, rather than defendants who "stand mute", proof of reliance is required. (*Ibid.*)*

Compare also the recent decision of the Court of Appeals for the Third Circuit in *Sharp* v. *Coopers & Lybrand*, No. 80-2229 (3d Cir. April 28, 1981), which adopts a third approach that presumes reliance "'where it is logical' to do so." (Slip op. at 24) In an action brought under § 10(b) against independent accountants based upon a published report the court held that there is no certain rule concerning proof of reliance, and expressly rejected the decision in *Huddleston* to "attempt to inject more certainty into the allocation of the burden of reliance." (Slip op. at 26 & n.19)

> "[T]he proper approach to the problem of reliance is to analyze the plaintiff's allegations, in light of the likely proof at trial, and determine the most reasonable placement of the burden of proof of reliance." (Slip op. at 26)

The court held that because of the "likelihood that investors would rely" in the circumstances of *Sharp*, reliance could be presumed. (Slip op. at 27)

---

* Although it said the § 10(b) remedy is an "established remedy", the court also defined the scienter standard in a § 10(b) action which it said is "presently uncertain" in "this circuit", defined for the first time the burden of proof of scienter and defined due diligence and loss causation elements of the cause of action. (640 F.2d at 544-48) Like the court of appeals below, its analysis paid no attention to the elements of any of the express causes of action under the federal securities laws.

The lower federal courts continue to treat §§ 10(b) of the 1934 Act and 17(a) of the 1933 Act as immune from the constitutionally premised standards enunciated by the Court in its recent decisions concerning the existence and dimensions of "implied" private causes of action. If there is to be such immunity, that determination should be made by the Court.

The anomaly presented by the lower courts' treatment of §§ 10(b) and 17(a) is further underscored by the Court's recent decisions in *Complete Auto Transit, Inc.* v. *Reis*, 49 U.S.L.W. 4473 (U.S. May 4, 1981), *California* v. *Sierra Club*, 49 U.S.L.W. 4441 (U.S. April 28, 1981), *City of Milwaukee* v. *Illinois*, 49 U.S.L.W. 4445 (U.S. April 28, 1981), *Northwest Airlines, Inc.* v. *Transport Workers Union*, 49 U.S.L.W. 4383 (U.S. April 20, 1981), and *Universities Research Ass'n* v. *Coutu*, 49 U.S.L.W. 4354 (U.S. April 6, 1981), which reiterate that "the focus of the inquiry is on whether Congress intended to create a remedy," *California* v. *Sierra Club*, 49 U.S.L.W. at 4444.

In contrast to the decision of the court below that Congressional "silence" concerning "the judicial implication of a private remedy" validates that cause of action (36a), the Court in *California* v. *Sierra Club*, 49 U.S.L.W. at 4444 n.7, rejected "legislative silence" as a basis for ascertaining Congressional intent.

Similarly, the court below rejected "[t]he ancient maxim '*expressio unius est exclusio alterius*'" as a "dangerous road map with which to explore legislative intent." (27a) The Court, however, reiterated in *Northwest Airlines, Inc.*, 49 U.S.L.W. at 4389, that:

> "The presumption that a remedy was deliberately omitted from a statute is strongest when Congress has enacted a comprehensive legislative scheme including an integrated system of procedures for enforcement."

Accord, Universities Research Ass'n v. *Coutu,* 49 U.S.L.W. at 4359 & n.24. The court of appeals said that a § 10(b) remedy could be implied in favor of Wachovia Bank because that is "the only true relief available to them" (35a), whereas in *California* v. *Sierra Club,* 49 U.S.L.W. at 4444, the Court held:

> "The federal judiciary will not engraft a remedy on a statute, no matter how salutary, that Congress did not intend to provide."

Accord, City of Milwaukee v. *Illinois,* 49 U.S.L.W. at 4447:

> "Federal courts, unlike state courts, are not general common law courts and do not possess a general power to develop and apply their own rules of decision. *Erie R. Co.* v. *Tompkins,* 304 U.S. 64, 78 (1938); *United States* v. *Hudson & Goodwin,* 11 U.S. (7 Cranch) 32 (1812). The enactment of a federal rule in an area of national concern, and the decision whether to displace state law in doing so, is generally made not by the federal judiciary, purposefully insulated from democratic pressures, but by the people through their elected representatives in Congress."

2. *Retroactivity.* The decision of the court of appeals denying retroactive application to its ruling in *Forrestal Village* is in conflict with the recent decision of the Court of Appeals for the Second Circuit in *Holzsager* v. *The Valley Hospital,* No. 80-7839 (2d Cir. April 10, 1981). In *Holzsager* the court held that a judicial ruling is to be given retroactive effect under *Chevron Oil Co.* v. *Huson,* 404 U.S. 97 (1971), even where the "decision reversed established law, so that [plaintiff] meets the first *Chevron* criterion. . . ." (Slip op. at 2499)

CONCLUSION

The writ of certiorari should issue.

Respectfully submitted,

WILLIAM E. HEGARTY
80 Pine Street
New York, New York 10005
(212) 825-0100

Counsel of Record

VICTOR M. EARLE, III
345 Park Avenue
New York, New York 10022

Attorneys for Petitioners

Of Counsel:

MATHIAS E. MONE
JOSEPH W. MUCCIA
CAHILL GORDON & REINDEL
80 Pine Street
New York, New York 10005

May 1981

Office-Supreme Court, U
F I L E D
MAY 21 1981
ALEXANDER L. STEVAS
CLERK

Nos. 80-1684, 80-1691, and 80-1802

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

PEAT, MARWICK, MITCHELL & CO., *et al.*, *Petitioners*,

v.

WACHOVIA BANK & TRUST CO., N. A., *et al.*, *Respondents*.

BRIEF FOR THE RESPONDENTS IN OPPOSITION

RICHARD M. PHILLIPS
CHERIF SEDKY
JONATHAN N. EISENBERG
HILL, CHRISTOPHER AND PHILLIPS, P.C.
1900 M Street, N.W.
Washington, D.C. 20036
(202) 452-7000

Attorneys for Respondents

May 1981

QUESTIONS PRESENTED

1. Whether a private action for fraud under Section 10(b) of the Securities Exchange Act of 1934 must be brought within the statutorily prescribed time for a private action for negligence under Section 12(2) of the Securities Act of 1933.

2. Whether fraud remedies under Section 10(b) are available only to sellers of securities and do not extend to defrauded purchasers.

3. Whether accountants and attorneys who actively participate in a fraud are excluded from the definition of "any person" in Section 10(b).

4. Whether fraudulent conduct not covered by express liability provisions of the federal securities laws is nevertheless also excluded from the coverage of the "catch-all" fraud provisions of Section 10(b).

5. Whether investors who participate in the securities markets through institutional fiduciaries are entitled to less protection under Section 10(b) than other investors.

6. Whether a decision overruling clear and previously controlling precedent by shortening the statute of limitations for bringing an action under Section 10(b) must be applied retroactively even when such application would be substantially inequitable.

TABLE OF CONTENTS

	PAGE:
OPINIONS BELOW	1
JURISDICTION	2
STATEMENT	2
ARGUMENT	9
CONCLUSION	24

TABLE OF AUTHORITIES

CASES:	PAGE
Aaron v. *SEC*, 446 U.S. 680 (1980)	9
Aboussie v. *Aboussie*, 441 F.2d 150 (5th Cir. 1971)	20
Adickes v. *S. H. Kress & Co.*, 398 U.S. 144 (1970)	10
Affiliated Ute Citizens v. *United States*, 406 U.S. 128 (1972)	9, 17
Andrus v. *Allard*, 444 U.S. 51 (1979)	14
Azalea Meats, Inc. v. *Muscat*, 246 F. Supp. 780 (S.D. Fla. 1965), rev'd on other grounds, 386 F.2d 5 (5th Cir. 1967)	20
Bailes v. *Colonial Press, Inc.*, 444 F.2d 1241 (5th Cir. 1971)	20
Baumel v. *Rosen*, 283 F.Supp. 128 (D. Md. 1968)	19
Berry Petroleum Co. v. *Adams & Peck*, 518 F.2d 402 (2d Cir. 1975)	21
Blau v. *Lehman*, 368 U.S. 403 (1962)	14
Blue Chip Stamps v. *Manor Drug Stores*, 421 U.S. 723 (1975)	9, 12, 14
Butterman v. *Steiner*, 343 F.2d 519 (7th Cir. 1965)	20
Cahill v. *Ernst & Ernst*, 625 F.2d 151 (7th Cir. 1980)	11
Campbell v. *Haverhill*, 155 U.S. 610 (1895)	11

PRECEDING PAGE WAS BLANK

Table of Authorities Continued

CASES: PAGE

Cannon v. *University of Chicago,* 441 U.S. 677 (1979) 9, 13

Carothers v. *Rice,* 633 F.2d 7 (6th Cir. 1980), cert. denied, 49 U.S.L.W. 3710 (Mar. 23, 1981) 11

Carpenter v. *Hall,* 311 F. Supp. 1099 (S.D. Tex. 1970) .. 20

Charney v. *Thomas,* 372 F.2d 97 (6th Cir. 1967) 20

Chevron Oil Co. v. *Huson,* 404 U.S. 97 (1971) 8, 21, 22

Chiodo v. *General Waterworks Corp.,* 380 F.2d 860 (10th Cir.), cert. denied, 389 U.S. 1004 (1967) 20

Conlow v. *University Computing Co.,* [1972-1973] Fed. Sec. L. Rep. (CCH) ¶ 93,796 (D.D.C. 1973) 21

Connelly v. *Balkwill,* 174 F. Supp. 49 (N.D. Ohio 1959), aff'd per curiam, 279 F.2d 685 (6th Cir. 1960) 20

Cook v. *Avien, Inc.,* 573 F.2d 685 (1st Cir. 1978) 11, 21

Cort v. *Ash,* 422 U.S. 66 (1975) 8

Dack v. *Shanman,* 227 F. Supp. 26 (S.D.N.Y. 1964) 19

deHaas v. *Empire Petroleum Co.,* 435 F.2d 1223 (10th Cir. 1970) 20

Denny v. *Performance Systems, Inc.,* [1971-1972] Fed. Sec. L. Rep. (CCH) ¶ 93,387 (M.D. Tenn. 1971) ... 20

Douglas v. *Glenn E. Hinton Investments, Inc.,* 440 F.2d 912 (9th Cir. 1971) 20

Dudley v. *Allen,* [1971-1972] Fed. Sec. L. Rep. (CCH) ¶ 93,273 (W.D. Ky. 1971) 20

Ernst & Ernst v. *Hochfelder,* 425 U.S. 185 (1976) 9, 10, 11

Errion v. *Connell,* 236 F.2d 35 (9th Cir. 1971) 20

Firestone Tire & Rubber Co. v. *Risjord,* 49 U.S.L.W. 4089 (Jan. 13, 1981) 23

Table of Authorities Continued

CASES:	PAGE
Fischman v. *Raytheon Manufacturing Co.*, 188 F.2d 783 (2d Cir. 1951)	19
Forrestal Village, Inc. v. *Graham*, 551 F.2d 411 (D.C. Cir. 1977)	8, *passim*
Fratt v. *Robinson*, 203 F.2d 627 (9th Cir. 1953)	20
Geo. H. McFadden & Brothers v. *Home-Stake Production Co.*, 295 F. Supp. 587 (N.D. Okla. 1968)	20
Glickman v. *Schweickart & Co.*, 242 F. Supp. 670 (S.D.N.Y. 1965)	19
Hecht v. *Harris, Upham & Co.*, 283 F. Supp. 417 (N.D. Cal. 1968), modified on other grounds, 430 F.2d 1202 (9th Cir. 1970)	20
Heit v. *Weitzen*, 402 F.2d 909 (2d Cir. 1968), cert. denied, 395 U.S. 903 (1969)	17
Hendricks v. *Flato Realty Investments*, [1967-1969] Fed. Sec. L. Rep. (CCH) ¶ 92,290 (S.D. Tex. 1968)	20
Hooper v. *Mountain States Securities Corp.*, 282 F.2d 195 (5th Cir. 1960), cert. denied, 365 U.S. 814 (1961)	20
Holzsager v. *The Valley Hospital*, No. 80-7839 (2d Cir. Apr. 10, 1981)	23
Hudak v. *Economic Research Analysts Inc.*, 499 F.2d 996 (5th Cir.), cert. denied, 419 U.S. 1122 (1974)	11
Huddleston v. *Herman & MacLean*, [Current] Fed. Sec. L. Rep. (CCH) ¶ 97,919 (5th Cir. 1981)	13
IIT v. *Cornfeld*, 619 F.2d 909 (2d Cir. 1980)	11
Janigan v. *Taylor*, 344 F.2d 781 (1st Cir.), cert. denied, 382 U.S. 879 (1965)	19
Johnson v. *Railway Express Agency, Inc.*, 421 U.S. 454 (1975)	11
Klein v. *Auchincloss, Parker & Redpath*, 436 F.2d 339 (2d Cir. 1971)	19

Table of Authorities Continued

CASES:	PAGE
Klein v. *Bower*, 421 F.2d 338 (2d Cir. 1970)	19
Klein v. *Spear, Leeds & Kellogg*, 306 F. Supp. 743 (S.D.N.Y. 1969)	19
Lehigh Valley Trust Co. v. *Central National Bank of Jacksonville*, 409 F.2d 989 (5th Cir. 1969)	18
Lorillard v. *Pons*, 434 U.S. 575 (1978)	14
Maher v. *J.R. Williston & Beane, Inc.*, 280 F. Supp. 133 (S.D.N.Y. 1967)	19
Marth v. *Industrial Incomes Incorporated of North America*, 290 F. Supp. 755 (S.D.N.Y. 1968)	19
McCluny v. *Silliman*, 28 U.S. (3 Pet.) 270 (1830)	11
Mills v. *Electric Auto-Lite Co.*, 396 U.S. 375 (1970)	18
Mitchell v. *Texas Gulf Sulphur Co.*, 446 F.2d 90 (10th Cir.), cert. denied, 404 U.S. 1004 (1971)	12, 20
Moerman v. *Zipco, Inc.*, 302 F. Supp. 439 (E.D.N.Y.), aff'd per curiam, 422 F.2d 871 (2d Cir. 1970)	19
Morgan v. *Koch*, 419 F.2d 993 (7th Cir. 1969)	20
National Realty Trust v. *Neelon Management Co.*, [1973] Fed. Sec. L. Rep. (CCH) ¶ 94,049 (D.D.C. 1973)	20-21
NLRB v. *Sears, Roebuck & Co.*, 421 U.S. 132 (1975)	18
Northern Trust Co. v. *Essaness Theatres Corp.*, 103 F. Supp. 954 (N.D. Ill. 1952)	20
Occidental Life Ins. Co. of California v. *EEOC*, 432 U.S. 355 (1977)	12
O'Hara v. *Kovens*, 625 F.2d 15 (4th Cir. 1980), cert. denied, 101 S.Ct. 939 (1981)	21
Osborne v. *Mallory*, 86 F. Supp. 869 (S.D.N.Y. 1949)	19
Parrent v. *Midwest Rug Mills, Inc.*, 455 F.2d 123 (7th Cir. 1972)	21

Table of Authorities Continued

CASES:	PAGE
Piper v. *Chris-Craft Industries, Inc.*, 430 U.S. 1 (1977)	9
Ramsey v. *United Mine Workers*, 401 U.S. 302 (1971)	18
Richardson v. *MacArthur*, 451 F.2d 35 (10th Cir. 1971)	20
Roberts v. *Magnetic Metals Co.*, 611 F.2d 450 (3rd Cir. 1979)	11
Ross v. *A.H. Robins Co.*, 607 F.2d 545 (2d Cir. 1979), cert. denied, 446 U.S. 946 (1980)	13, 16, 17
Royal Air Properties, Inc. v. *Smith*, 312 F.2d 210 (9th Cir. 1962)	20
Rubin v. *United States*, 101 S.Ct. 698 (1981)	18
Sackett v. *Beaman*, 399 F.2d 884 (9th Cir. 1968)	20
Santa Fe Industries, Inc. v. *Green*, 430 U.S. 462 (1977)	9
Saylor v. *Lindsley*, 302 F. Supp. 1174 (S.D.N.Y. 1969)	19
Schaefer v. *First National Bank of Lincolnwood*, 326 F. Supp. 1186 (N.D. Ill. 1971)	20
Schaefer v. *First National Bank of Lincolnwood*, 509 F.2d 1287 (7th Cir. 1975), cert. denied, 425 U.S. 943 (1976)	22
SEC v. *National Securities Co.*, 393 U.S. 453 (1969)	18
SEC v. *National Student Marketing Corp.*, 457 F. Supp. 682 (D.D.C. 1978)	2, 6
Shapiro v. *Schwamm*, 279 F. Supp. 798 (S.D.N.Y. 1968)	19
Smith v. *Guaranty Service Corp.*, 51 F.R.D. 289 (N.D. Cal. 1970)	20
Stevens v. *Abbott, Proctor & Paine*, 288 F. Supp. 836 (E.D. Va. 1968)	20
Superintendent of Insurance v. *Bankers Life & Casualty Co.*, 404 U.S. 6 (1971)	9, 17
Tobacco & Allied Stocks, Inc. v. *Transamerica Corp.*, 143 F. Supp. 323 (D. Del. 1956), aff'd without consideration of the point, 244 F.2d 902 (3rd Cir. 1957)	19

Table of Authorities Continued

CASES: PAGE

Touche Ross & Co. v. *Redington,* 442 U.S. 560 (1979) 8, 9, 14

Transamerica Mortgage Advisors, Inc. v. *Lewis,* 444 U.S. 11 (1979) 8, 14

Trussell v. *United Underwriters, Ltd.,* 228 F. Supp. 757 (D. Colo. 1964) 20

Turner v. *Lundquist,* 377 F.2d 44 (9th Cir. 1967) 20

UAW v. *Hoosier Cardinal Corp.,* 383 U.S. 696 (1966) .. 11

United California Bank v. *Salik,* 481 F.2d 1012 (9th Cir.), cert. denied, 414 U.S. 1004 (1973) 11

United States v. *Naftalin,* 441 U.S. 768 (1979) 17, 18

United States v. *Natelli,* 527 F.2d 311 (2d Cir. 1975), cert. denied, 425 U.S. 934 (1976) 2, 4

Valencia v. *Anderson Brothers Ford,* 617 F.2d 1278 (7th Cir.), cert. granted, 101 S.Ct. 395 (1980) 23

Vance v. *National Realty Trust,* [1974-1975] Fed. Sec. L. Rep. (CCH) ¶ 95,004 (D.C. Cir. 1975) 20

Vanderboom v. *Sexton,* 422 F.2d 1233 (8th Cir.), cert. denied, 400 U.S. 852 (1970) 11

Weinberger v. *New York Stock Exchange,* 335 F. Supp. 139 (S.D.N.Y. 1971) 19

Weiser v. *Shwartz,* 286 F.Supp. 389 (E.D. La. 1968) 20

STATUTES:

Investment Advisers Act of 1940 §206, 15 U.S.C. 80b-6 14

Securities Act of 1933

§11, 15 U.S.C. 77k 11

§12, 15 U.S.C. 77l ..... 7, *passim*

§17, 15 U.S.C. 77q 18

Table of Authorities Continued

STATUTES: PAGE

Securities Exchange Act of 1934

§3(a)(9), 15 U.S.C. 78c(a)(9) 15

§10(b), 15 U.S.C. 78j(b) ..... 3, *passim*

§17, 15 U.S.C. 78q 14

§18, 15 U.S.C. 78r ..... 7, *passim*

MISCELLANEOUS:

H.R. Conf. Rep. No. 1838, 73d Cong., 2d Sess. (1934).. 15

R. Stern & E. Gressman, Supreme Court Practice (5th ed. 1978) 23

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

Nos. 80-1684, 80-1691, and 80-1802

PEAT, MARWICK, MITCHELL & CO., *et al., Petitioners,*

v.

WACHOVIA BANK & TRUST CO., N. A., *et al., Respondents.*

BRIEF FOR THE RESPONDENTS IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A)[1] is not yet officially reported. The opinion of the district court in Nos. 80-1684 and 80-1691 (Pet. App. B) is reported at 461 F.

---

[1] Unless otherwise indicated, the designation "Pet." refers to the petition for a writ of certiorari in No. 80-1691. The designation "Pet. App." refers to the appendix in that petition.

Supp. 999. The opinion of the district court in No. 80-1802 (No. 80-1802, Pet. App. A) is not officially reported.

JURISDICTION

The judgment of the court of appeals was entered on December 5, 1980. Petitions for rehearing and suggestions for rehearing *en banc* were denied on March 4, 1981. (Pet. App. C). Petitions for a writ of certiorari were filed on April 7, 1981, April 8, 1981, and April 29, 1981. The jurisdiction of this court is invoked under 28 U.S.C. §1254(1).

STATEMENT

This case arises from the financial debacle of the National Student Marketing Corporation ("NSMC") in the late 1960's. Following that debacle, successful criminal actions were brought against certain officers of NSMC and a partner of the accounting firm in this action (Petitioner Natelli).[2] In addition, an SEC injunctive action resulted in consent judgments against the Petitioners now before this Court.[3] Nevertheless, for nearly a decade the victims of the fraud have been deprived of their day in court. Petitioners now attempt to make that deprivation permanent by seeking certiorari from the refusal of the court of appeals to uphold dismissal of the complaint in this action.

Respondents, plaintiffs below, are Wachovia Bank and Trust Co., N. A., Mellon Bank, N. A., First Wisconsin Trust

---

[2] *See United States* v. *Natelli*, 527 F.2d 311 (2d Cir. 1975), cert. denied, 425 U.S. 934 (1976). Petitioner Scansaroli, the other individual accountant in this action, also was indicted and was convicted of violations of the federal securities laws in this matter. However, his conviction was overturned on appeal. The court of appeals found that there was sufficient evidence to convict Scansaroli of criminal law violations, but that it could not be determined if the jury had in fact convicted him of a violation for which there was insufficient evidence. Mr. Scansaroli was never re-tried after remand.

[3] *See SEC* v. *National Student Marketing Corp.*, 457 F. Supp. 682, 687 n.2 (D.D.C. 1978).

Co., the Dreyfus Offshore Trust, N. V. and National Fire Insurance Co. of Hartford. On December 17, 1969, they purchased more than $5 million of NSMC stock from NSMC and two of its directors in a private placement. Three of the five Respondents purchased their NSMC shares as fiduciaries for employee retirement plans and other trust accounts. The price was negotiated from the prevailing market to reflect long term restrictions against resale. The stock turned out to be virtually worthless.

Petitioners, defendants below, are Peat, Marwick, Mitchell & Co. ("PMM"), a national accounting firm that regularly acted as NSMC's independent auditors; Anthony M. Natelli, the PMM partner in charge of the NSMC account; Joseph Scansaroli, PMM's audit supervisor of the NSMC account; White & Case, a New York law firm that regularly represented NSMC as outside counsel and served as such in connection with the private placement involving the Respondents; Marion Jay Epley, III, the White & Case partner principally responsible for the NSMC account; and certain former NSMC officers and directors. NSMC was also named as a defendant in the original complaint; however, it subsequently settled with the plaintiffs.

Respondents' complaint, as amended, alleges that the Petitioners violated and aided and abetted violations of Section 10(b) in connection with NSMC's dissemination of false and misleading statements in the marketplace. These false statements, going to the very heart of NSMC's financial condition, were disseminated to investors orally, in press releases, and in numerous public announcements and reports. The great majority were made orally and in documents that were not filed with the SEC (Complaint, Paras. 22, 24, 25, 26, 30, 31, 53, 55, 57, 59, 63, 66, 69). Their effect was to inflate artificially the price of NSMC stock, which was then used fraudulently to acquire numerous profitable corporations. The earnings of these corporations were then pooled with NSMC's to mask the fact that NSMC itself was losing money at a staggering rate.

The accounting Petitioners and the attorney Petitioners were not mere peripheral defendants caught up in a fraudulent scheme of which they had no knowledge. Rather, they were critical participants in that scheme who knew what was transpiring and deliberately chose to further the deception of their client.

Through late 1968, NSMC's scheme to defraud was accomplished principally through the booking of revenues from so called "commitments" to purchase NSMC services ("unbilled sales"). These commitments were first booked in connection with NSMC's 1968 year end audit when PMM learned that a trial balance showed more than a $200,000 loss for the year. PMM then allowed NSMC retroactively to book $1.7 million of revenues from "commitments" even though (1) not a single dollar from these commitments was received prior to year end; (2) PMM did not confirm the existence of the commitments with NSMC's customers; and (3) PMM knew that there were no written contracts for virtually all of the commitments. When in 1969 the great majority of the commitments had failed to materialize and had to be written off, PMM concealed the effect of these write-offs by permitting NSMC to substitute a series of new non-existent commitments. As the Second Circuit found in *United States* v. *Natelli*, 527 F.2d 311, 319 (2d Cir. 1975), cert. denied, 425 U.S. 934 (1976):

> "The original action of Natelli in permitting the booking of unbilled sales after the close of the fiscal period in an amount sufficient to convert a loss into a profit was contrary to sound accounting practice. . . . When the uncollectibility, and indeed, the non-existence of these large receivables was established in 1969, the revelation stood to cause Natelli severe criticism and possible liability. He had a motive, therefore, intentionally to conceal the write-offs that had to be made."

PMM, notwithstanding its knowledge of the fraud, rendered unqualified opinions upon NSMC's financial statements and assisted in the preparation of NSMC's interim financial

statements which it knew were false. For that reason, NSMC was able to report dramatic increases in sales and earnings from one accounting period to the next even though such sales and earnings increases were wholly chimerical.

The widespread dissemination of false reports of increasing sales and earnings served to excite the market and artificially inflate the price of NSMC stock. In less than two years NSMC stock climbed from $6 a share to $144 a share even though the company was in fact losing money during this entire period.[4] By early 1969, however, NSMC was unable to generate enough fraudulent "commitments" to maintain its reports of spectacular growth. Accordingly, it embarked on a series of fraudulent corporate acquisitions in which it used its inflated stock and false financial statements to purchase profitable companies. NSMC then pooled the earnings of the profitable companies with its own and thereby concealed the write-offs of commitments that had failed to materialize.

During NSMC's corporate acqusition program, Respondents purchased for cash more than $5 million of NSMC stock. The purchases were effected through Common Stock Purchase Agreements. Under the agreements, Respondents' obligation to purchase NSMC shares was conditioned on receipt from White & Case of a legal opinion to the effect that, among other things, consummation of the transaction would not result in a violation of any statute, rule or regulation. White & Case and Epley rendered such legal opinions to each of the Respondents without any qualification.

In fact, as Epley well knew, the sales to Respondents resulted in numerous violations of the securities laws because they were based on false representations. Epley knew of the fraud because he had been a central participant in the fraudulent transactions which gave rise to the false representations.

---

[4] The $144 figure takes into account a two-for-one stock split.

For example, Epley had served as NSMC's counsel in the October 1969 merger of Interstate National Corporation into NSMC — the principal subject of the SEC's enforcement action in *SEC* v. *National Student Marketing Corp.*, 457 F. Supp. 682 (D.D.C. 1978). There, prior to the closing, the head of PMM's SEC Review Committee called Epley to advise him that NSMC's most recent nine-month financials must be corrected to show a $180,000 loss instead of the $700,000 profit shown in the financial statements used to obtain shareholder approval of the merger. Epley declined to inform Interstate of this development, but falsely represented to PMM that he had discussed the matter with Interstate and Interstate still wanted to go forward. The merger was closed only on Epley's fraudulent representation to Interstate that an unsigned, incomplete draft comfort letter from PMM regarding the most recent nine-month financials was in fact final and complete, and that a signed copy would be forthcoming from PMM. The final comfort letter, which Epley never disclosed to Interstate, not only contained the qualification that NSMC had lost $180,000, but also stated that Interstate should consider a resolicitation of shareholders with corrected financials prior to closing.

The following month Epley and White & Case represented NSMC in three more fraudulent acquisitions. In each instance, White & Case prepared representations that the nine-month financials — which Epley knew from the Interstate transaction were false — were "true and correct" and "prepared in accordance with generally accepted accounting principles." At no time did Epley disclose the infirmities with the Interstate acquisition to the companies that were later being acquired on the basis of Interstate earnings. As a result, NSMC was able to use its false financial statements and inflated stock to perpetuate its fraud by acquiring new companies with profits that could be used to conceal NSMC's losses in NSMC's consolidated financial statements. Of course, the paper empire that NSMC had built with the assistance of its professional advisers was largely dismantled

through a series of rescission actions instituted after the fraud was discovered.

In the courts below the defendants urged that no private right of action exists under Section 10(b) of the Securities Exchange Act for the fraud charged. They argued that recognition of a claim under Section 10(b) would "nullify the express provisions of the 1933 Act" (PMM Court of Appeals Brief, p. 67), and that "an Implied Right of Action Does Not Lie Since the Conduct in Issue Is Subject to §18 [of the Securities Exchange Act]" (id at 68). Defendants also moved to dismiss the action as time-barred under the District of Columbia's two-year blue-sky statute of limitations. Defendants' motion to dismiss was made more than four years after the filing of plaintiffs' complaint, by which time no fewer than 166 witnesses had been deposed and plaintiffs had been compelled to produce, copy and analyze literally hundreds of thousands of documents.

The district court rejected defendants' contention that no claim for relief was stated under Section 10(b). It found that plaintiffs were alleging a cause of action far different from that addressed by Section 12(2) of the Securities Act or Section 18(a) of the Securities Exchange Act — the two express provisions defendants relied upon to argue there was no claim under Section 10(b). With respect to Section 18(a), the court noted that "plaintiffs have alleged materially false statements which were never contained in a document filed with the SEC and thus are clearly exempt from §18(a) liability" (Pet. App. B-8). Further, "[w]ith limited exceptions, plaintiffs do not allege reliance upon documents filed with the SEC and, contrary to the position of defendants, such reliance is essential to recovery under §18(a)" (ibid). With respect to Section 12(2), the court stated that victims of intentional fraud are not limited to the Section 12(2) negligence remedy, and further that "there is some question whether [Section 12(2)] applies to the present defendants since they were not 'sellers' of the securities in question" (id at B-8).

The district court, however, dismissed the complaint as time-barred under the District of Columbia's two-year blue sky statute of limitations. The court relied on the 1977 decision of the District of Columbia Circuit in *Forrestal Village, Inc.* v. *Graham*, 551 F.2d 411 (1977), which broke with past precedent and applied the two-year blue-sky limitation period instead of the three-year general fraud limitation period. At the time plaintiffs had filed their complaint in January 1973, the three year general fraud statute applied to Section 10(b) actions brought in the District of Columbia.

The court of appeals reversed the dismissal. With respect to the existence of a private right of action under Section 10(b), the court noted that in the last decade this Court has acknowledged that a private right of action exists under Section 10(b) in no less than six cases (Pet. App. A-18 and n. 21). It found that such recognition was consistent with the four-part test in *Cort* v. *Ash*, 422 U.S. 66, 78 (1975), and that neither *Touche Ross & Co.* v. *Redington*, 442 U.S. 560 (1979) nor *Transamerica Mortgage Advisors, Inc.* v. *Lewis*, 444 U.S. 11 (1979) compelled a different result. It rejected what it characterized as defendants' "Catch 22" argument based on express remedies, noting that although defendants urged that the existence of express remedies precluded a remedy under Section 10(b), "in each instant [defendants] are at the ready to show that the express remedies are not really available to Wachovia" (Pet. App. A-26). It further pointed out that these express remedies "are totally different from the remedy implied under Section 10(b), and . . . are meant to treat different problems and to be applied in different situations" (Pet. App. A-27).

On the question of prospective application of the statute of limitations decision, the court followed this Court's decision in *Chevron Oil Co.* v. *Huson*, 404 U.S. 97 (1971). It found that its *Forrestal Village* decision overruled the law in the District of Columbia Circuit at the time plaintiffs filed the complaint, that the three-year general fraud statute applied to Section 10(b) actions. It noted that as of the time the lower

court found the blue sky limitation period had expired, forty-six of forty-eight federal court decisions had applied the forum state's general fraud statute of limitations to Section 10(b) actions, and that as late as 1975 — two years after the complaint was filed — D. C. decisions were still applying the three year general fraud statute to Section 10(b) actions. It found that to hold that Respondents slept on their rights would produce "substantial inequitable results," since they could not have known that the statute of limitations in effect at the time they filed their complaint would be shortened in a decision still years down the road.

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this court or any other court of appeals. Further review is therefore unwarranted.

1. The court of appeals created no new remedy. Rather it reconfirmed the well-established private claim for relief under Section 10(b). That claim has been recognized in countless federal court decisions over the last thirty-five years, and has been confirmed by this Court in numerous recent decisions.[5] Further, the court of appeals did not extend Section 10(b) to a new class of plaintiffs, to a new type of fraud, or to a new category of defendants. It held only that purchasers of securities who are victims of a massive but essentially garden-variety fraud have a remedy under Section 10(b) against persons who, acting with *scienter*, make materially false and

[5] *See Aaron* v. *SEC*, 446 U.S. 680, 689 (1980); *Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 569, 577 n.19 (1979); *Cannon* v. *University of Chicago*, 441 U.S. 677, 692 n.13, 706 n.40 (1979); *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 477 (1977); *Piper* v. *Chris-Craft Industries, Inc.*, 430 U.S. 1, 25 (1977); *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 196 (1976); *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 730 (1975); *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 144-154 (1972); *Superintendent of Insurance* v. *Bankers Life & Casualty Co.*, 404 U.S. 6, 13 n.9 (1971).

misleading representations in connection with the sale of securities.

Petitioners attack the lower court's recognition of a Section 10(b) remedy on several grounds. None reflects a conflict in the circuits or a conflict with any decision of this Court.

2. The attorney Petitioners principally argue that purchasers should not to able to bring a fraud action under Section 10(b) once the time has expired for bringing a negligence action under Section 12(2) of the Securities Act, a section which does not even apply to them. (Pet. i, 11-16). This novel argument was not addressed by the lower courts because Petitioners did not there advance it. In the lower courts, Petitioners argued that the D.C. blue-sky limitation period governs, not the statute of limitations that governs Section 12(2). Ordinarily, a litigant will not be heard to assert in this Court contentions which it did not raise below. See, e.g., *Adickes* v. *S.H. Kress & Co.*, 398 U.S. 144, 147 n.2 (1970).

Further, Petitioners' argument in this Court is simplistic. They contend that the Section 10(b) remedy nullifies the procedural constraints in Section 12(2) because a longer statute of limitation could be applied to Section 10(b). Petitioners ignore, however, that Section 10(b) and Section 12(2) treat different problems and apply in different situations; hence, reliance on the former does not in any way nullify or undermine the latter. This is particularly true where, as here, the Petitioners are not even sellers and thus cannot be reached by a Section 12(2) action.

Section 10(b) is directed to fraud, and a plaintiff who elects to proceed under Section 10(b) undertakes the burden of proving *scienter*. *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185 (1976). Section 12(2) is simply a misrepresentation statute. *Scienter* is irrelevant, and indeed a plaintiff can establish a prima facie case by simply showing a misrepresentation and forcing the defendants to prove an affirmative defense of non-negligence.

Given the burden on a plaintiff in a Section 10(b) action to prove *scienter*, it can hardly be argued that recognition of an action under Section 10(b) would nullify Section 12(2). Indeed, in *Ernst & Ernst* v. *Hochfelder, supra*, 425 U.S. at 210, this Court recognized that imposition of a *scienter* requirement under section 10(b) was necessary to avoid nullification of the procedural restrictions in Section 12(2), as well as in the other express remedies of the securities laws.[6]

Further, Petitioners ignore the fact that for more than a century this Court has instructed lower courts that where no federal statute of limitations is provided for a particular cause of action, the federal courts are not to borrow other federal limitation periods but are to utilize the appropriate limitation period of the forum state.[7] In *Hochfelder*, this Court noted that such use of state statutes of limitations is the practice in Section 10(b) cases. 425 U.S. at 210 n. 29. Every single court of appeals in the federal system applies state limitation periods to Section 10(b) actions.[8]

---

[6] The express remedies of the securities laws generally place the burden on the defendant to prove absence of culpability. See, e.g., Sections 11(b) and 12(2) of the Securities Act and Section 18(a) of the Securities Exchange Act.

[7] *See, e.g., Johnson* v. *Railway Express Agency, Inc.*, 421 U.S. 454, 462 (1975); *UAW* v. *Hoosier Cardinal Corp.*, 383 U.S. 696, 701-704 (1966); *Campbell* v. *Haverhill*, 155 U.S. 610, 621 (1895); *McCluny* v. *Silliman*, 28 U.S. (3 Pet.) 270, 277 (1830).

[8] *Cook* v. *Avien, Inc.*, 573 F.2d 685, 694 (1st Cir. 1978); *IIT* v. *Cornfeld*, 619 F.2d 909, 928 (2d Cir. 1980); *Roberts* v. *Magnetic Metals Co.*, 611 F.2d 450, 452 (3d Cir. 1979); *O'Hara* v. *Kovens*, 625 F.2d 15, 18 (4th Cir. 1980), cert. denied, 101 S.Ct. 939 (1981); *Hudak* v. *Economic Research Analysts Inc.*, 499 F.2d 996, 999 (5th Cir.), cert. denied, 419 U.S. 1112 (1974); *Carothers* v. *Rice*, 633 F.2d 7, 12-15 (6th Cir. 1980), cert. denied, 49 U.S.L.W. 3710 (Mar. 23, 1981); *Cahill* v. *Ernst & Ernst*, 625 F.2d 151, 153 (7th Cir. 1980); *Vanderboom* v. *Sexton*, 422 F.2d 1233, 1237 (8th Cir.), cert. denied, 400 U.S. 852 (1970); *United California Bank* v. *Salik*, 481 F.2d 1012, 1014 (9th Cir.), cert. denied, 414 U.S. 1004 (1973);

Petitioners' reliance on *Occidental Life Ins. Co. of California* v. *EEOC*, 432 U.S. 355 (1977) for the proposition that state statutes of limitation should not be applied is wholly misplaced. *Occidental*, which is not a securities case, held that where the state statute of limitations was so short that it defeated the federal substantive policy, no statute of limitations would be applied at all. Hence, *Occidental* is not authority for borrowing federal statutes of limitations, but for rejecting all such statutes — a result that Petitioners hardly seek. Further, *Occidental* turned on the unique fact that the fundamental substantive federal policies of conciliation and voluntary settlement, on which Title VII of the Civil Rights Act was premised, would be defeated if a state one-year statute of limitations were imposed in Title VII cases. No remotely comparable situation is involved here.

3. Petitioners also urge that certiorari should be granted so that this Court can hold that only defrauded sellers but not defrauded purchasers, such as the plaintiffs, have a remedy under Section 10(b). In essence, they believe that the clock should be turned back 35 years and Section 10(b), the "judicial oak which has grown from little more than a legislative acorn" [*Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 737 (1975)], should be returned to its status as an acorn.

The arguments which Petitioners contrive, however, prove too much. There is no basis in the language of Section 10(b), its legislative history, or in the decisions interpreting it for distinguishing between defrauded purchasers and defrauded sellers. Either Petitioners must seek repeal of Section 10(b) altogether for victims of fraud, or they must urge that it be eviscerated without any regard to consistency or rational distinctions.

Mitchell v. *Texas Gulf Sulphur Co.*, 446 F.2d 90, 103 (10th Cir.), cert. denied, 404 U.S. 1004 (1971); *Forrestal Village, Inc.*, v. *Graham*, 551 F.2d 411, 413 (D.C. Cir. 1977).

Petitioners simply cannot escape the significance of this Court's repeated confirmation of a private claim for relief under Section 10(b).[9] The Court in these decisions was hardly unaware of the considerations on which Petitioners rely to deny a remedy here. The Court recognized a remedy under Section 10(b) because for 35 years, without the slightest hint of Congressional disapproval, lower court interpretations had made Section 10(b) the most important and widely utilized private remedy under the securities laws. This longstanding acceptance by the courts of the role of Section 10(b), coupled with Congress' failure to disturb these decisions, argued significantly in favor of continued recognition of a limited remedy under Section 10(b). It is this factor which distinguishes Section 10(b) from recent decisions in which this Court has declined to create *new* private rights of action under other sections of the federal securities laws.[10]

Indeed, only recently this Court recognized in connection with Section 10(b) that it "has frequently accepted a history of federal court recognition of a cause of action as indicative of the propriety of its implication." *Cannon* v. *University of*

---

[9] See note 5, *supra*.

[10] Petitioners and the amicus mischaracterize this case as representative of an expansionist interpretation of the securities laws by the lower courts. The decision, however, is even more narrow than that of the Second Circuit in *Ross* v. *A.H. Robins Co.*, 607 F.2d 545 (2d Cir. 1979), cert. denied, 446 U.S. 946 (1980), in which this Court denied a petition for a writ of certiorari. In *Ross*, the Second Circuit recognized a claim for relief under Section 10(b) for misrepresentations in filed documents, the very documents which may give rise to Section 18(a) liability. Here, by contrast, the majority of the misrepresentations alleged were made in unfiled documents and orally, where Section 18(a) does not apply. The decision is also narrower than the Fifth Circuit's decision in *Huddleston* v. *Herman & MacLean*, [Current] Fed. Sec. L. Rep. (CCH) ¶ 97,919 (1981). There, the court recognized a claim for relief under Section 10(b) for misrepresentations contained in a prospectus even though plaintiffs could have brought their claims under Section 11 of the Securities Act.

Chicago, 441 U.S. 677, 706 n.40 (1979). In *Touche Ross & Co.* v. *Redington, supra,* 442 U.S. at 577 n.19, the Court refused to accept the longstanding recognition of implied remedies under Section 10(b) as grounds for implying a similar remedy under Section 17(a) of the Securities Exchange Act because in the case of the latter, "There is no similar history of longstanding lower court interpretation in this case." The absence of such a longstanding history of lower court interpretation also provides a basis for distinguishing this Court's decision in *Transamerica Mortgage Advisors, Inc.* v. *Lewis, supra,* refusing to recognize an implied remedy for damages under Section 206 of the Investment Advisers Act of 1940.

The Court's treatment of Section 10(b) is consistent with its long-standing view that "Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change." *Lorillard* v. *Pons,* 434 U.S. 575, 580 (1978). *See also, Andrus* v. *Allard,* 444 U.S. 51, 57 (1979); *Blue Chip Stamps* v. *Manor Drug Stores, supra,* 421 U.S. at 733-734; *Blau* v. *Lehman,* 368 U.S. 403, 413 (1962). Congress has revisited and amended the securities laws on countless occasions since it became evident that lower courts were implying private rights of action under Section 10(b). Not once did it suggest any disagreement with this approach of the courts.

Petitioners would like nothing more than for this Court to turn its back on four decades of judicial interpretation of Section 10(b) and to leave victims of one of the most massive stock frauds in the last decade without any remedy against persons who actively and knowingly participated in the fraud. There is no basis for such action in this Court's most recent decisions. In rejecting new private rights of action, the Court's decisions have nevertheless made clear that the Court has not abandoned the longstanding recognition of a private claim for relief for fraud under Section 10(b).

4. Petitioners and the amicus assert that this Court should grant certiorari to hold that claims may not be asserted under Section 10(b) against lawyers and accountants because such persons would be liable as "so-called aiders and abettors" and not as sellers of securities (Pet. 20). Such an assertion erroneously assumes that Petitioners are charged with liability under Section 10(b) as either sellers or aiders and abettors and in no other capacity. The attorneys and accountants in this case are charged in the complaint not only as aiders and abettors but also as principal violators who played a central role in the scheme to defraud and who themselves made material misrepresentations in connection with the sale of securities. Thus the issue raised by Petitioners — whether lawyers and accountants can be liable as aiders and abettors under Section 10(b) — is prematurely raised. When Respondents have their day in court, it may well be that aiding and abetting plays no role at all in this case.

Petitioners claim that there is no statutory basis in Section 10(b) for prohibiting fraud by accountants and attorneys who are not sellers. They ignore the very obvious statutory basis: Section 10(b) is not limited to sellers; it proscribes conduct by "any person" who "directly or indirectly" engages in the prohibited conduct. There is no special exemption for lawyers and accountants from the definition of "person."[11]

Petitioners would have this Court ignore the literal language of the statute because of purported concern about the danger of vexatious litigation against attorneys and accountants. Such a concern is especially ironic in this case. This is a case in which the two individual accountants were criminally prosecuted, in which all of the Petitioners were

---

[11] Section 3(a)(9) of the Act defines person to include "a natural person." Further, Section 18(a) of the Act, which also relies on "any person" language, was originally drafted to cover "any person (including any director or officer, or any accountant or other expert.)" The parenthetical clause was deleted in conference because "[t]he words in parentheses are . . . superfluous." H.R. Conf. Rep. 1838, 73rd Cong., 2d Sess. 36 (1934).

subject to SEC enforcement proceedings, and in which all consented to judgments against them. Further, a district court opinion and an appellate opinion in related cases strongly suggest egregious fraud by these same Petitioners. Nevertheless, these Petitioners criticize the Plaintiffs — all institutional investors which for the most part are acting in a representative capacity — for bringing a vexatious action and in the same breath attempt to bar this action as untimely because Petitioners investigated and deliberated too long before filing suit.

Finally, there is no circuit court conflict on the issues that Petitioners seek to raise. Petitioners are unable to point to a single decision supporting their contention that Section 10(b) affords a special dispensation to professionals who engage in fraudulent conduct or even that aiding and abetting liability does not lie under Section 10(b).

5. In the court of appeals, the accounting Petitioners argued that "If the 1934 Act Applies, an Implied Right of Action under §10(b) Does Not Lie Since the Conduct in Issue Is Subject to §18 [of the Securities Exchange Act]" (PMM Br. 68). Now, both the accounting Petitioners and the amicus AICPA argue that because Section 18(a) does not provide a remedy to Respondents, no claim can be stated under Section 10(b). That is why the court of appeals characterized Petitioners' arguments as a "Catch 22." Petitioners believe that if the express provisions provide a remedy for the fraud, then the victims of the fraud should not be permitted to proceed under Section 10(b), but if the express provisions do not provide a remedy for the fraud, that is even more reason to deprive them of a remedy under Section 10(b).

Petitioners' argument rests on a misunderstanding of the different purposes served by Section 18(a) and Section 10(b). Section 18(a) provides a remedy for deception resulting from eyeball reliance on documents filed with the SEC. See, e.g., *Ross* v. *A.H. Robins Co.*, 607 F.2d 545, 552 (2d Cir. 1979), cert. denied, 446 U.S. 946 (1980). It is designed to insure the integrity of corporate reports filed with the SEC and relied

upon by purchasers of securities. In contrast, Section 10(b) is not designed to protect the integrity of filed documents; it is designed to protect against frauds perpetrated on purchasers and sellers of securities through false representations, which are often made in unfiled documents and in oral statements. Thus, Section 18(a) does not, as Petitioners argue, serve to insulate from Section 10(b) liability persons who choose to defraud the public through, for example, press releases, public announcements and reports disseminated to investors that are not required to be filed with the SEC.

Further, Petitioners' argument that Section 10(b) cannot be used where a Section 18(a) claim does not lie is refuted by the decisions of this Court recognizing Section 10(b) claims where filed documents were not even at issue. See *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128 (1972); *Superintendent of Insurance* v. *Bankers Life & Casualty Co.,* 404 U.S. 6 (1971). The reliance of the complaint principally on false representations disseminated in unfiled documents removes any doubt that a claim for relief is stated under Section 10(b).

Nor is it significant that some of the misrepresentations made in unfiled documents were also made in filed documents. Section 18(a) requires eyeball reliance on the filed documents. *Ross* v. *A.H. Robins Co., supra,* 607 F.2d at 552; *Heit* v. *Weitzen,* 402 F.2d 909, 916 (2d Cir. 1968), cert. denied, 395 U.S. 903 (1969). Persons who are defrauded through widely disseminated fraudulent unfiled documents are not deprived of a Section 10(b) remedy simply because they did not read the filed documents containing the same misrepresentations. And, even if there were some overlap in remedies afforded by Section 10(b) and Section 18(a) — a factor which is not present in this case to the extent no reliance is claimed on the filed misrepresentations — the Section 10(b) claim would not be defeated. As this Court repeatedly has recognized, the fact that there may be some overlap between the various provisions of the securities laws is neither unusual nor unfortunate. *United States* v. *Naftalin,* 441 U.S. 768,778

(1979); *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 390-391 (1970): *SEC* v. *National Securities Co.*, 393 U.S. 453, 468 (1969).

6. Petitioners in No. 80-1802 urge that even if small unsophisticated investors would have a remedy under Section 10(b), in the circumstances of this case Respondents should not because they are "sophisticated institutional investors" (Pet. 4). Petitioners ignore, however, that the protections and remedies of the securities laws "are not accorded only to those who fail a battery of information and intelligence tests, but are simply conditioned upon the misrepresentation of material facts." *Lehigh Valley Trust Co.* v. *Central National Bank of Jacksonville,* 409 F.2d 989, 992 (5th Cir. 1969). There is no statutory or decisional support for Petitioners' wholly impractical interpretation of Section 10(b). To the contrary, this Court's decisions make abundantly clear that the antifraud proscriptions of the securities laws are as much for the protection of the sophisticated as for the unsophisticated. See, e.g., *Rubin* v. *United States,* 101 S.Ct. 698 (1981); *United States* v. *Naftalin,* 441 U.S. 768 (1979).

In *Naftalin,* this Court recognized that "the welfare of investors and financial intermediaries are inextricably linked — frauds perpetrated upon either business or investors can redound to the detriment of the other and to the economy as a whole." 441 U.S. at 776. Here, Respondents purchased for the most part as trustees for numerous small unsophisticated investors. Whatever restrictions are placed on Section 10(b) ultimately will redound to the detriment of such investors.[12]

---

[12] Petitioners in No. 80-1684 seek to raise the question whether a private claim for relief may be stated under Section 17(a) of the Securities Act. The court of appeals, however, did not decide that question, and it is therefore inappropriate for consideration on a writ of certiorari. *NLRB* v. *Sears, Roebuck & Co,* 421 U.S. 132, 163-164 (1975); *Ramsey* v. *United Mine Workers,* 401 U.S. 302, 312 (1971).

7. Petitioners urge that certiorari should be granted to determine whether the court of appeals erred in refusing to apply its decision in *Forrestal Village Inc.* v. *Graham,* 551 F.2d 411 (D.C. Cir. 1977) retroactively. That decision held that the D.C. two-year blue sky statute of limitations, rather than the three year general fraud limitation, applies to Section 10(b) cases.

The issue raised by Petitioners is not worthy of certiorari. Supreme Court resolution of this issue would have no effect on future cases because the law on the statute of limitations question has changed drastically in the last decade. The court of appeals decision was premised on the fact that as of December 1971 — the time the district court found the two year blue sky limitation period expired for Plaintiffs in this action — forty-six of forty-eight federal court decisions had applied the forum state's general fraud statute to Section 10(b) actions[13], and this was the law in the District of Colum-

---

[13] The court of appeals relied upon the following pre-1972 decisions: *First Circuit: Janigan* v. *Taylor,* 344 F.2d 781, cert. denied, 382 U.S. 879 (1965); *Second Circuit: Klein* v. *Auchincloss, Parker & Redpath* 436 F.2d 339 (1971); *Klein* v. *Bower,* 421 F.2d 338 (1970); *Moerman* v. *Zipco, Inc.,* 302 F. Supp. 439 (E.D.N.Y. 1970), *aff'd per curiam,* 422 F.2d 871 (1970); *Fischman* v. *Raytheon Manufacturing Co.,* 188 F.2d 783 (1951); *Weinberger* v. *New York Stock Exchange,* 335 F.Supp. 139 (S.D.N.Y. 1971); *Klein* v. *Spear, Leeds & Kellogg,* 306 F.Supp. 743 (S.D.N.Y. 1969); *Saylor* v. *Lindsley,* 302 F.Supp. 1174 (S.D.N.Y. 1969); *Marth* v. *Industrial Incomes Incorporated of North America,* 290 F.Supp. 755 (S.D.N.Y. 1968); *Shapiro* v. *Schwamm,* 279 F.Supp. 798 (S.D.N.Y. 1968); *Maher* v. *J.R. Williston & Beane, Inc.,* 280 F.Supp. 133 (S.D.N.Y. 1967); *Glickman* v. *Schweickart & Co.,* 242 F.Supp. 670 (S.D.N.Y. 1965); *Dack* v. *Shanman,* 227 F.Supp. 26 (S.D.N.Y. 1964); *Osborne* v. *Mallory,* 86 F.Supp. 869 (S.D.N.Y. 1949); *Third Circuit: Tobacco & Allied Stocks, Inc.* v. *Transamerica Corp.,* 143 F.Supp. 323 (D. Del. 1956), aff'd without consideration of the point, 244 F.2d 902 (1957); *Fourth Circuit: Stevens* v. *Abbott, Proctor & Paine,* 288 F.Supp. 836 (E.D.Va. 1968); *Baumel* v.

bia (ibid). Thus, the court noted that "prior to, and during, the running of the limitations period, federal courts, including this circuit, overwhelmingly adopted the general fraud limita-

---

Rosen, 283 F.Supp. 128 (D. Md. 1968); *Fifth Circuit: Bailes* v. *Colonial Press, Inc.,* 444 F.2d 1241 (1971); *Aboussie* v. *Aboussie,* 441 F.2d 150 (1971); *Weiser* v. *Shwartz,* 286 F.Supp. 389 (E.D.La. 1968); *Azalea Meats, Inc.,* v. *Muscat,* 246 F.Supp. 780 (S.D.Fla. 1965), rev'd on other grounds, 386 F.2d 5 (1967); *Hooper* v. *Mountain States Securities Corp.,* 282 F.2d 195 (1960), cert. denied, 365 U.S. 814 (1961); *Carpenter* v. *Hall,* 311 F.Supp. 1099 (S.D.Tex. 1970); *Hendricks* v. *Flato Realty Investments,* [1967-1969 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 92,290 (S.D.Tex. 1968); *Sixth Circuit: Charney* v. *Thomas,* 372 F.2d 97 (1967); *Connelly* v. *Balkwill,* 174 F.Supp. 49 (N.D. Ohio, 1959), aff'd per curiam, 279 F.2d 685 (1960); *Denny* v. *Performance Systems, Inc.,* [1971-1972] Fed.Sec.L.Rep. (CCH) ¶ 93,387 (M.D. Tenn. 1971); *Dudley* v. *Allen* [1971-1972] Fed.Sec.L.Rep. (CCH) ¶ 93,273 (W.D. Ky. 1971); *Seventh Circuit: Morgan* v. *Koch,* 419 F.2d 993 (1969); *Butterman* v. *Steiner,* 343 F.2d 519 (1965); *Schaefer* v. *First National Bank of Lincolnwood,* 326 F.Supp. 1186 (N.D. Ill. 1971); *Northern Trust Co.* v. *Essaness Theatres Corp.,* 103 F.Supp. 954 (N.D. Ill. 1952); *Ninth Circuit: Douglass* v. *Glenn E. Hinton Investments, Inc.,* 440 F.2d 912 (1971); *Sackett* v. *Beaman,* 399 F.2d 884 (1968); *Hecht* v. *Harris, Upham & Co.,* 283 F.Supp. 417 (N.D.Cal. 1968), modified on other grounds, 430 F.2d 1202 (1970); *Turner* v. *Lundquist,* 377 F.2d 44 (1967); *Royal Air Properties, Inc.,* v. *Smith,* 312 F.2d 210 (1962); *Errion* v. *Connell,* 236 F.2d 35 (1971); *Fratt* v. *Robinson,* 203 F.2d 627 (1953); *Smith* v. *Guaranty Service Corp.,* 51 F.R.D. 289 (N.D. Cal. 1970); *Tenth Circuit: Richardson* v. *MacArthur,* 451 F.2d 35 (1971); *Mitchell* v. *Texas Gulf Sulphur Company,* 446 F.2d 90, cert. denied, 404 U.S. 1004 (1971); *deHaas* v. *Empire Petroleum Co.,* 435 F.2d 1223 (1970); *Chiodo* v. *General Waterworks Corp.,* 380 F.2d 860, cert. denied, 389 U.S. 1004 (1967); *Geo. H. McFadden & Brothers* v. *Home-Stake Production Co.,* 295 F.Supp. 587 (N.D. Okla. 1968); *Trussell* v. *United Underwriters, Ltd.,* 228 F.Supp. 757 (D. Colo. 1964). As late as 1975, courts in the D.C. Circuit reaffirmed that the three-year general fraud limitation applies to Section 10(b) action. See, e.g., *Vance* v. *National Realty Trust,* [1974-1975] Fed.Sec.L.Rep. (CCH) ¶ 95,004 (D.C. Cir. 1975); *National Realty Trust* v. *Neelon Management*

tion period" (Pet. App. A-13). This was the basis for its determination that, as to the Plaintiffs in this action, *Forrestal Village* established a new principle of law. It was also the basis for its conclusion that it would be inequitable to hold that Respondents slept on their rights since at the time they filed their complaint the three-year statute of limitations clearly applied.

Since 1971 the lower courts have reconsidered the question, and the certainty that existed a decade ago has disappeared. In the last decade the lower courts have divided sharply on whether state blue sky or fraud limitations apply to Section 10(b) actions.[14] As a result, no plaintiff filing a complaint today or even in the last five years could claim, as was the case here, that a decision applying a blue sky limitation period was wholly unforeshadowed or marked a sharp departure from earlier decisions. Thus, this Court's resolution of the issue posed by Petitioners would be limited to the facts and the parties in this particular case.

Further, the court of appeals decision is correct on the merits. This case is at least as compelling for nonretroactivity as *Chevron Oil Co.* v. *Huson* 404 U.S. 97 (1971). *Chevron*, like the instant case, involved the question whether retroactive application should be given to a decision that effectively applied a state one-year limitation period to actions for injuries sustained on the Outer Continental Shelf. The Court found

---

Co., [1973] Fed.Sec.L.Rep. ¶ 94,049 (D.D.C. 1973); *Conlow* v. *University Computing Co.*, [1972-1973] Fed.Sec.L.Rep. (CCH) ¶ 93,796 (D.D.C. 1973).

[14] Compare, e.g., *O'Hara* v. *Kovens*, 625 F.2d 15 (4th Cir. 1980), cert. denied, 101 S.Ct. 939 (1981); *Forrestal Village, Inc.* v. *Graham*, 551 F.2d 411 (D.C. Cir. 1977); *Berry Petroleum Co.* v. *Adams & Peck*, 518 F.2d 402 (2d Cir. 1975); *Parrent* v. *Midwest Rug Mills, Inc.*, 455 F.2d 123 (7th Cir. 1972) (applying blue sky limitation periods) with, e.g., *Roberts* v. *Magnetic Metals Co.*, 611 F.2d 450 (3rd Cir. 1979) and *Cook* v. *Avien, Inc.*, 573 F.2d 685 (1st Cir. 1978) (applying general fraud limitation periods).

that the decision should be applied prospectively because (1) it overruled prior law on which plaintiff had relied in determining when to bring the action; (2) it would undermine the protective purposes of the statute in issue to deprive an injured person of a remedy on the basis of superseding legal doctrine that was not foreseeable; and (3) it would be substantially inequitable to hold that the plaintiff had slept on his rights since at the time he filed his action the existing law was that his action was timely. Quoting from an earlier decision, this Court emphasized that "[w]here a decision of this Court could produce substantial inequitable results if applied retroactively, there is ample basis in our cases for avoiding the 'injustice or hardship' by a holding of nonretroactivity." *Id.* at 107.

In the decision below, the court of appeals found, as in *Chevron,* that its *Forrestal Village* decision changed the law in the D.C. Circuit as it existed at the time Respondents filed their complaint. It also found that it would be substantially inequitable to hold that Respondents slept on their rights on the basis of a decision rendered four years after they filed their complaint. Petitioners complain that the court below did not also find that the second factor mentioned in *Chevron* had been met. The second factor was in fact met: the purposes of the securities laws are indeed undermined when victims of fraud are deprived of a remedy on the basis of unforeseen changes in the law. In any event, *Chevron* only requires that the three factors be "considered," not that each be met. 404 U.S. at 106.

Finally, the decision of the court of appeals does not create any conflict with the decisions of any other court of appeals. The attorney Petitioners rely on *Schaefer* v. *First National Bank of Lincolnwood,* 509 F.2d 1287 (7th Cir. 1975), cert. denied, 425 U.S. 943 (1976). That case, however, was brought in the Seventh Circuit and the Seventh Circuit held that the decision in question did not overturn prior law in the Seventh Circuit. 509 F.2d at 1294-1295. Here the action was brought in the District of Columbia and the D.C. Circuit

specifically found that its *Forrestal Village* decision did overturn prior D.C. Circuit law. Further, in *Schaefer* retroactive application of the statute of limitations had little effect on plaintiffs' claims; more than two dozen defendants remained in the case even under the shorter statute of limitations. Here, application of the shorter statute of limitations would defeat Respondents' claims in their entirety.

The accounting Petitioners attempt to create a conflict in the circuits by relying upon *Valencia* v. *Anderson Brothers Ford,* 617 F.2d 1278 (7th Cir.), cert. granted, 101 S.Ct. 395 (1980) and *Holzsager* v. *The Valley Hospital,* No. 80-7839 (2d Cir. Apr., 1981). They ignore, however, that a conflict can justify review only if there is "a real conflict on the same matter of law or fact, not merely an inconsistency in *dicta* or in the general principles utilized." R. Stern & E. Gressman, Supreme Court Practice 264 (5th ed. 1978).

The decisions on which the accounting Petitioners rely are not even securities decisions, much less Section 10(b) decisions, and they raise no issues regarding retroactive application of statutes of limitations decisions. *Valencia* held only that a particular interpretation of the Truth in Lending Act would be applied retroactively because, unlike this case, the court concluded that the interpretation was supported by the weight of prior authority. The suggestion that all three *Chevron* factors must be met was only in *dicta,* and unlike in *Valencia,* where the court did not find that any of the *Chevron* factors had been met, all three factors were in fact met here. *Holzsager* applied a jurisdictional decision retroactively even though that decision changed existing law, but as the concurring judge noted in that case, jurisdictional decisions have always been applied retroactively [citing this Court's decision in *Firestone Tire & Rubber Co.* v. *Risjord,* 49 U.S.L.W. 4089, 4092 (Jan. 13, 1981)].

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

RICHARD M. PHILLIPS
CHERIF SEDKY
JONATHAN N. EISENBERG
HILL, CHRISTOPHER AND PHILLIPS, P.C.
1900 M Street, N.W.
Washington, D.C. 20036
(202) 452-7000

Attorneys for Respondents

May 1981

No. 80-1684

MAY 23 1981

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

PEAT, MARWICK, MITCHELL & Co.,
ANTHONY M. NATELLI and JOSEPH SCANSAROLI,
Petitioners,

v.

WACHOVIA BANK AND TRUST Co., N.A., MELLON BANK, N.A., FIRST WISCONSIN TRUST Co., THE DREYFUS OFFSHORE TRUST, N.V., and NATIONAL FIRE INSURANCE Co. OF HARTFORD,
Respondents.

REPLY BRIEF IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

WILLIAM E. HEGARTY
80 Pine Street
New York, New York 10005
(212) 825-0100
Counsel of Record

VICTOR M. EARLE, III
345 Park Avenue
New York, New York 10022
Attorneys for Petitioners

Of Counsel:
MATHIAS E. MONE
JOSEPH W. MUCCIA
CAHILL GORDON & REINDEL
80 Pine Street
New York, New York 10005

May 1981

TABLE OF CONTENTS

PAGE

1. The "implied" remedy 1

2. Retroactivity 8

CONCLUSION 9

TABLE OF AUTHORITIES

Cases:

Aaron v. *SEC*, 446 U.S. 680 (1980) 4

Affiliated Ute Citizens v. *United States*, 406 U.S. 128 (1972) 4

Chevron Oil Co. v. *Huson*, 404 U.S. 97 (1971) 8

Erie R. Co. v. *Tompkins*, 304 U.S. 64 (1938) 5

Helvering v. *Hallock*, 309 U.S .106 (1940) 5-6

New York Transit Authority v. *Beazer*, 440 U.S. 568 (1979) 2-3

Northwest Airlines, Inc. v. *Transport Workers Union*, 49 U.S.L.W. 4383 (U.S. April 20, 1981) 3

Santa Fe Industries, Inc. v. *Green*, 430 U.S. 462 (1977) 4

SEC v. *National Securities, Inc.*, 393 U.S. 453 (1969) 4, 5

Superintendent of Insurance v. *Bankers Life & Casualty Co.*, 404 U.S. 6 (1971) 4

Texas Industries, Inc. v. *Radcliff Materials, Inc.*, —— U.S. —— (No. 79-1144, May 26, 1981) 2

Touche Ross & Co. v. *Redington*, 442 U.S. 560 (1979) 7

Transamerica Mortgage Advisors, Inc. v. *Lewis*, 444 U.S. 11 (1979) 3-4

PAGE

United States v. *Natelli*, 527 F.2d 311 (2d Cir. 1975), *cert. denied*, 425 U.S. 934 (1976) 7

Congressional Documents:

H. R. Rep. No. 2513, 84th Cong., 2d Sess. (1956) 6

Statutes:

Investment Advisers Act of 1940
§ 206, 15 U.S.C. § 80b-6 (1976) 4

Securities Act of 1933
§ 16, 15 U.S.C. § 77p (1976) 7n
§ 17(a), 15 U.S.C. § 77q(a) (1976) ..... *passim*

Securities Exchange Act of 1934
§ 10(b), 15 U.S.C. § 78j(b) (1976) ..... *passim*
§ 28(a), 15 U.S.C. § 78bb(a) (1976) 7n

Law Reviews:

L. Loss, *History of S.E.C. Legislative Programs and Suggestions for a Code*, 22 Bus. Law 795 (1967) 2

Other:

R. Phillips & M. Miller, *The Demise of Implied Rights*, 13 Review of Securities Reg. 887 (1980) 3

No. 80-1684

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

PEAT, MARWICK, MITCHELL & CO.,
ANTHONY M. NATELLI and JOSEPH SCANSAROLI,

Petitioners,

v.

WACHOVIA BANK AND TRUST CO., N.A., MELLON BANK, N.A., FIRST WISCONSIN TRUST CO., THE DREYFUS OFFSHORE TRUST, N.V., and NATIONAL FIRE INSURANCE CO. OF HARTFORD,

Respondents.

REPLY BRIEF IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

1. *The "implied" remedy.* The response of Wachovia Bank scarcely acknowledges the question presented by the PMM petition:

> May a federal court create a damage remedy under § 17(a) of the Securities Act of 1933 or § 10(b) of the Securities Exchange Act of 1934 for purchasers of securities who cannot establish the elements of any of the express causes of action which those Acts provide injured purchasers?

The Court should once and for all settle whether private damage remedies which have been "implied" under §§ 17(a) and 10(b) need not have their source in Congressional intent, although the Court has made the intent of Congress

the Constitutional touchstone for the determination of whether a private remedy may properly be inferred from a statute which provides none.

Just this week the Court said in *Texas Industries, Inc.* v. *Radcliff Materials, Inc.*, —— U.S. —— (No. 79-1144, May 26, 1981), at p. 8, that "Our focus, as it is in any case involving the implication of a right of action, is on the intent of Congress." The Court held that federal courts are without authority "to formulate what has come to be known as 'federal common law'" when, as here, what is at issue "involv[es] the rights and obligations of private parties" and "[t]here is nothing in the statute itself, in the legislative history, or in the overall regulatory scheme to suggest that Congress intended courts to have the power to alter or supplement the remedies enacted." (*Id.* at pp. 10, 12, 15)

The court of appeals took no account of Congressional intent. Instead, it provided a remedy because no express remedy was available (33a, 35a). Such rulings have been aptly characterized by Professor Loss:

> "What has happened to Rule 10b-5 . . . always reminds me of a cartoon of the time showing Mussolini dictating to his secretary, and the caption was, 'Miss Baccigalupi, take a law.'" L. Loss, *History of S.E.C. Legislative Programs and Suggestions for a Code*, 22 Bus. Law. 795, 796 (1967).

Wachovia Bank says inaccurately that the question presented is "inappropriate" insofar as it relates to § 17(a) of the 1933 Act because the court of appeals did not decide that question. (Wachovia Bank Br. 18 n.12) The question was decided by the district court (49a), and it was raised by PMM in the court of appeals (17a-18a). The Court held in *New York Transit Authority* v. *Beazer*, 440

U.S. 568, 583 n. 24 (1979): "The failure of the Court of Appeals to address the statutory issue decided by the District Court does not, of course, prevent this Court from reaching the issue. Cf. *University of California Regents* v. *Bakke*, 438 U.S. 265." *Accord, Northwest Airlines, Inc.* v. *Transport Workers Union*, 49 U.S.L.W. 4383, 4385 & n.15 (U.S. April 20, 1981).

Counsel for Wachovia Bank has written of the § 17(a) question, R. Phillips & M. Miller, *The Demise of Implied Rights*, 13 Review of Securities Reg. 887, 889 (1980):

> "Because these express causes of action [under the 1933 Act] are limited in scope and present certain disadvantages to plaintiffs—for example, a relatively short statute of limitations—those bringing suit have often argued that an action for damages should be implied by the courts [*sic*] under section 17(a). While the lower courts have been divided, the Supreme Court has yet to address this question. However, the issue has apparently been resolved by the Court's analysis in *Transamerica*. Congress expressly authorized private suits for damages under section 12(2) for purchasers of securities offered or sold in violation of section 17(a); '[o]bviously, then when Congress wished to provide a private damage remedy, it knew how to do so and did so expressly.'
>
> "Like section 206 of the Investment Advisers Act, section 17(a) outlaws fraudulent conduct but it 'does not in terms create or alter any civil liabilities.' Accordingly, under the *Transamerica* analysis, evidence of congressional intent weighs against the implication of a private right of action in a case brought under section 17(a)." (Footnote omitted)

It is difficult to distinguish § 10(b) from § 17(a) and, as observed in the dissent in *Transamerica Mortgage*, 444

U.S. 11, 25 n.1 (1979), "The provisions of § 206 of the Investment Advisers Act of 1940, 15 U.S.C. § 80b-6, are substantially similar to § 10(b) of the Securities Exchange Act of 1934." How then can judicial implication of a § 10(b) remedy be justified?

The Court said in *Santa Fe Industries, Inc.* v. *Green,* 430 U.S. 462, 477 (1977), that it has "recognized an implied cause of action under [§ 10(b)] in some circumstances." In fact, the Court has sustained a § 10(b) remedy, without analysis, in two cases, *Superintendent of Insurance* v. *Bankers Life & Casualty Co.,* 404 U.S. 6 (1971), and *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128 (1972). Both involved sellers who, in contrast to purchasers, have no cause of action under the 1933 Act. Whether a private cause of action may properly be inferred from § 10(b) of the 1934 Act was not raised in either case or in any other case decided by the Court. The Court said in *Aaron* v. *SEC,* 446 U.S. 680, 689, 691 (1980), that a private damage action "was not within the contemplation of the Congress that enacted § 10(b)" and that it has "assumed" the existence of the implied cause of action.

Wachovia Bank says "[p]etitioners simply cannot escape the significance of this Court's repeated confirmation of a private claim for relief under Section 10(b)" (Wachovia Bank Br. 13). This is not only a grievous exaggeration but precisely the sort of "unthinking abstraction" against which the Court warned in *SEC* v. *National Securities, Inc.,* 393 U.S. 453, 465 (1969).

> "[T]his is the first time this Court has found it necessary to interpret [§ 10(b)]. We enter this virgin territory cautiously. The questions presented are narrow ones. They arise in an area where glib generalizations and unthinking abstractions are major occupational

> hazards. Accordingly, in deciding this particular case, remembering what is not involved is as important as determining what is." (*Ibid.*)

Wachovia Bank relies upon *National Securities* as support for "overlapping" of remedies under the federal securities laws (Wachovia Bank Br. 17-18). The Court, however, carefully pointed out in *National Securities* that "[t]his case presents none of the complications which may arise in determining who, if anyone, may bring private actions under § 10(b) . . . . This is a suit brought by the Commission." (393 U.S. at 467 n.9)

Wachovia Bank says the writ should not issue because "for 35 years, without the slightest hint of Congressional disapproval, lower court interpretations had made Section 10(b) the most important and widely utilized private remedy under the securities laws" (Wachovia Bank Br. 13) and because the remedy implied by lower courts is "totally different" from the express remedies enacted by Congress (*id.* at 8). These assertions only beg the question presented by the PMM petition.

Post-enactment Congressional "silence" concerning the lower court decisions does not provide the answer to the question. As the Court said in *Helvering* v. *Hallock*, 309 U.S. 106, 119-20 (1940):

> "It would require very persuasive circumstances enveloping Congressional silence to debar this Court from reexamining its own doctrines. To explain the cause of non-action by Congress when Congress itself sheds no light is to venture into speculative unrealities."

Congressional silence will not support the judicial lawmaking at issue here. *See also Erie R. Co.* v. *Tompkins*, 304 U.S. 64, 79-80 (1938):

"The fallacy underlying the rule declared in *Swift* v. *Tyson* is made clear by Mr. Justice Holmes. The doctrine rests upon the assumption that . . . federal courts have the power to use their judgment as to what the rules of common law are; and that in the federal courts 'the parties are entitled to an independent judgment on matters of general law':

'but law in the sense in which courts speak of it today does not exist without some definite authority behind it, . . .'

"Thus the doctrine of *Swift* v. *Tyson* is, as Mr. Justice Holmes said, 'an unconstitutional assumption of powers by courts of the United States which no lapse of time or respectable array of opinion should make us hesitate to correct.' In disapproving that doctrine we do not hold unconstitutional § 34 of the Federal Judiciary Act of 1789 or any other Act of Congress. We merely declare that in applying the doctrine this Court and the lower courts have invaded rights which in our opinion are reserved by the Constitution to the several States." (Footnote omitted)

Congress did not intend in 1934 to "imply" the remedy which the court of appeals ruled is available to Wachovia Bank. Neither the court of appeals nor Wachovia Bank point to any evidence that Congress thereafter considered and approved such a remedy. To the contrary, Congress explicitly recognized in 1956 that "there is no civil liability" in the circumstances alleged by Wachovia Bank, *H. R. Rep. No. 2513,* 84th Cong., 2d Sess. at 5 (1956) (*see* PMM Petition pp. 15-16), and as demonstrated in the brief of the American Institute of Certified Public Accountants as *amicus curiae* (pp. 17-18) the SEC advised Congress

in 1959 that there is no private civil liability for aiding and abetting a violation of the federal securities laws.

Wachovia Bank relies upon the rationale of the court of appeals that to deny a federal remedy in this case would leave respondents "without any remedy" (Wachovia Bank Br. 14) and devotes considerable energy to attempting to prove the wrong they have alleged (*id.* at 2-9). The argument that a remedy should be "implied" because a wrong was allegedly done is only a reiteration of the common law statutory tort concept rejected by the Court in *Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 576-78 (1979).*

The "successful criminal action" against Mr. Natelli to which Wachovia Bank refers (Wachovia Bank Br. 2) related to a misstatement in NSMC financial statements contained in its 1969 proxy statement, filed with the SEC. *United States* v. *Natelli*, 527 F.2d 311 (2d Cir. 1975), *cert. denied*, 425 U.S. 934 (1976). Wachovia Bank disclaimed reliance (34a) and did not institute this action until "well beyond the time allowed" by Congress in connection with any express remedy based upon the proxy statement (29a).**

---

* Wachovia Bank, moreover, ignores common law remedies available under state law, although Congress recognized in §§ 16 of the 1933 Act and 28(a) of the 1934 Act that the express remedies are in addition to any remedies available at common law.

** The conviction was based, moreover, upon a finding of recklessness. The trial judge said of Mr. Natelli on the record:

> "I think you are absolutely sincere when you say that you did not believe that you did anything wrong on this audit or audits for National Student Marketing. After thinking about this matter for a long time, I think you honestly mean that. But the tragedy is that the jury found that this was an audit or audits [which] were reckless."

Mr. Natelli has received a Presidential pardon, and he has been readmitted to practice as a certified public accountant before the Securities and Exchange Commission.

The record in this case precisely defines the question concerning the existence and dimensions of "implied" remedies under §§ 10(b) and 17(a). The question is vital and unresolved. It should be settled.

2. *Retroactivity.* The second question is:

> May a litigant avoid the retroactive effect of a previous decision when he is unable to show that all three factors of *Chevron Oil Co.* v. *Huson*, 404 U.S. 97 (1971), favor prospective-only effect?

Wachovia Bank asserts that "Supreme Court resolution of this issue would have no effect on future cases because the law on the statute of limitations question has changed drastically in the last decade." (Wachovia Bank Br. 19) The assertion is a *non sequitur*. More important, it incorrectly assumes that resolution of the question concerning the meaning of *Chevron Oil* would have effect only upon statutes of limitations issues.

If, as happened here, a court may deny retroactive effect to a decision based upon fewer than all of the *Chevron* factors, precedent ceases to have meaning. Wachovia Bank acknowledges a conflict among the circuits (Wachovia Bank Br. 23) on the question presented by the PMM petition.

The second question is an important federal question as to which there is a conflict among the circuits.

CONCLUSION

The writ of certiorari should issue.

Respectfully submitted,

WILLIAM E. HEGARTY
80 Pine Street
New York, New York 10005
(212) 825-0100
Counsel of Record

VICTOR M. EARLE, III
345 Park Avenue
New York, New York 10022
Attorneys for Petitioners

Of Counsel:

MATHIAS E. MONE
JOSEPH W. MUCCIA
CAHILL GORDON & REINDEL
Office & P.O. Address:
80 Pine Street
New York, New York 10005

May 1981

Office Supreme Court, U.S.
FILED
MAY 21 1981
ALEXANDER L. STEVAS,
CLERK

Nos. 80-1684/1691

IN THE

Supreme Court of the United States

October Term, 1980

PEAT, MARWICK, MITCHELL & CO., *et al.*,

Petitioners,

v.

WACHOVIA BANK AND TRUST CO., N.A., *et al.*,

Respondents.

WHITE & CASE AND MARION JAY EPLEY, III,

Petitioners,

v.

WACHOVIA BANK AND TRUST CO., N.A., *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA

BRIEF OF AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS AS *AMICUS CURIAE* IN SUPPORT OF THE PETITIONS FOR A WRIT OF CERTIORARI

KENNETH J. BIALKIN
LOUIS A. CRACO
HOWARD C. BUSCHMAN III
Attorneys for American Institute of Certified Public Accountants
One Citicorp Center
153 East 53rd Street
New York, New York 10022
(212) 935-8000

Of Counsel

WILLKIE FARR & GALLAGHER
MITCHELL J. AUSLANDER
One Citicorp Center
153 East 53rd Street
New York, New York 10022
(212) 935-8000

QUESTIONS PRESENTED

The American Institute of Certified Public Accountants confines its present participation to urging the Court to grant the Writ to review and decide at least the following issues which are subsumed by certain of the questions presented in the Petitions for Certiorari.

1. May a private cause of action for damages be implied under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1976) ("1934 Act") in favor of a purchaser of securities who is unable to satisfy the criteria for asserting the express causes of action provided by Section 18 of that Act?

2. May a private cause of action for damages be implied under Section 10(b) of the 1934 Act against a person who is alleged to be an aider and abettor of a violation of the Section?

TABLE OF CONTENTS

	PAGE
PRELIMINARY STATEMENT	1
QUESTIONS PRESENTED	2
INTEREST OF THE INSTITUTE AS *Amicus Curiae*	3
SUMMARY OF ARGUMENT	4
REASONS FOR GRANTING THE WRIT	5
A. The Holding Below Is Representative Of A Trend Of Lower Court Decisions Which Disregard The Limitations On Implied Causes Of Action Announced By This Court	5
B. It Was Error To Imply A Cause Of Action Under Section 10(b) In Favor Of Purchasers Who Were Unable To Obtain Relief Under Section 18 Of The 1934 Act	10
C. Private Causes Of Action For Aiding And Abetting Violations Of Section 10(b) Of The 1934 Act Should Not Be Implied	14
CONCLUSION	19

TABLE OF AUTHORITIES

PAGE

Cases

Aaron v. *SEC*, 446 U.S. 680 (1980) ..... 3, *passim*

Affiliated Ute Citizens v. *United States*, 406 U.S. 128 (1972) 7, 10

A.H. Robins Co., Inc. v. *Ross*, 446 U.S. 946 (1980) 3 n.3

Blue Chip Stamps v. *Manor Drug Stores*, 421 U.S. 723 (1975) ..... 6 n.4, *passim*

Brennan v. *Midwestern United Life Insurance Co.*, 259 F. Supp. 673 (N.D. Ind. 1966) 15, 17

California v. *Sierra Club*, —U.S.—, 49 U.S.L.W. 4441 (April 28, 1981) ..... 7, *passim*

Cannon v. *University of Chicago*, 441 U.S. 677 (1979) 7 n.6, 9, 16

City Nat'l Bank v. *Vanderboom*, 422 F.2d 221 (8th Cir.), *cert. denied*, 399 U.S. 905 (1970) 8 n.7

Clement A. Evans & Co. v. *McAlpine*, 434 F.2d 100 (5th Cir. 1970), *cert. denied*, 402 U.S. 988 (1971) 8 n.7

Daniel v. *International Brotherhood of Teamsters*, 561 F.2d 1223 (7th Cir. 1977), *rev'd on other grounds*, 439 U.S. 551 (1979) 9

Dupuy v. *Dupuy*, 551 F.2d 1005 (5th Cir.), *cert. denied*, 434 U.S. 911 (1977) 8, 8 n.8

Edwards & Hanly v. *Wells Fargo Securities Clearance Corp.*, 602 F.2d 478 (2d Cir. 1979), *cert. denied*, 444 U.S. 1045 (1980) 16

Ernst & Ernst v. *Hochfelder*, 425 U.S. 185 (1976)..3, *passim*

Healey v. *Catalyst Recovery of Pa., Inc.*, 616 F.2d 641 (3d Cir. 1980) 6 n.5

Hirsch v. *du Pont*, 553 F.2d 750 (2d Cir. 1977) 8 n.7

Holdsworth v. *Strong*, 545 F.2d 687 (10th Cir. 1976), *cert. denied*, 430 U.S. 955 (1977) 8 n.8

Huddleston v. *Herman & MacLean*, 640 F.2d 534 (5th Cir. 1981) 6 n.5

IIT v. *Cornfeld*, 619 F.2d 909 (2d Cir. 1980) 16 n.12

PAGE

International Brotherhood of Teamsters v. *Daniel*, 439 U.S. 551 (1979) 6 n.4

Kardon v. *National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa. 1946) 9, 15 n.11

Kirshner v. *United States*, 603 F.2d 234 (2d Cir. 1978), *cert. denied*, 442 U.S. 909 (1979) 9

Kissinger v. *Reporters Committee*, 445 U.S. 136 (1980) 7, 10

Landy v. *FDIC*, 486 F.2d 139 (3d Cir. 1973), *cert. denied*, 416 U.S. 960 (1974) 15, 16 n.12

Mallis v. *Bankers Trust Co.*, 615 F.2d 68 (2d Cir. 1980) 8 n.8

Mansbach v. *Prescott, Ball & Turben*, 598 F.2d 1017 (6th Cir. 1979) 6 n.5, 7

Milwaukee v. *Illinois*, —U.S.—, 49 U.S.L.W. 4445 (April 28, 1981) 7

National Railroad Passenger Corp. v. *National Ass'n of Railroad Passengers*, 414 U.S. 453 (1974) 10

Nelson v. *Serwold*, 576 F.2d 1332 (9th Cir.), *cert. denied*, 439 U.S. 970 (1978) 7 n.5

Newman v. *Prior*, 518 F.2d 97 (4th Cir. 1975) 9

Rochez Bros., Inc. v. *Rhoades*, 491 F.2d 402 (3d Cir. 1974), *cert. denied*, 425 U.S. 993 (1976) 8 n.7

Rolf v. *Blyth, Eastman Dillon & Co., Inc.*, 570 F.2d 38 (2d Cir.), *cert. denied*, 439 U.S. 1039 (1978) 7 n.5, 16 n.12

Santa Fe Industries, Inc. v. *Green*, 430 U.S. 462 (1977) 11

SEC v. *Coffey*, 493 F.2d 1304 (6th Cir. 1974), *cert. denied*, 420 U.S. 908 (1975) 16 n.12

SEC v. *Sloan*, 436 U.S. 103 (1978) 7

Straub v. *Vaisman & Co.*, 540 F.2d 591 (3d Cir. 1976) 8 n.8

Superintendent of Insurance v. *Bankers Life and Casualty Co.*, 404 U.S. 6 (1971) 10, 15

Sunstrand Corp. v. *Sun Chemical Corp.*, 553 F.2d 1033 (7th Cir.), *cert. denied*, 434 U.S. 875 (1977) .. 7 n.5, 8 n.8

Touche Ross & Co. v. *Redington*, 442 U.S. 560 (1979) ..... 3, *passim*

PAGE

Transamerica Mortgage Advisors v. *Lewis*, 444 U.S. 11 (1979) ..... 7 n.6, *passim*

Universities Research Ass'n v. *Coutu*, —U.S.—, 49 U.S.L.W. 4354 (April 6, 1981) ..... 7 n.6, *passim*

Wachovia Bank and Trust Co., N.A. v. *National Student Marketing Corp.*, 461 F. Supp. 999 (D.D.C. 1978) .. 6 n.4, 9

Woodward v. *Metro Bank of Dallas*, 522 F.2d 84 (5th Cir. 1975) 16 n.12

Statutes

Securities Act of 1933

§ 11, 15 U.S.C. § 77k (1976) 12 n.10

§ 15, 15 U.S.C. § 77o (1976) 17

§ 17, 15 U.S.C. § 77q (1976) 6 n.4

§ 17(a), 15 U.S.C. § 77q(a) (1976) 9

Securities Exchange Act of 1934

§ 10(b), 15 U.S.C. § 78j(b) (1976) ..... 2, *passim*

§ 18, 15 U.S.C. § 78r (1976) ..... 4, *passim*

§ 20(a), 15 U.S.C. § 78t (1976) 17

18 U.S.C. § 2 (1976) 18 n.13

Legislative Materials

78 CONG. REC. 7701, 8040 (1934) 12

H.R. REP. NO. 1383, 73d Cong., 2d Sess. (1934) 12 n.9

S. REP. NO. 792, 73d Cong., 2d Sess. (1934) 12 n.9

Hearings on S. Res. 84 (72d Cong.), S. Res. 56 and S. Res. 97 (73d Cong.) Before the Senate Committee on Banking and Currency, 73d Cong., 1st Sess., pt. 15 (1934) .. 3, 12

Hearings on S.1178-S.1182 Before a Subcommittee of the Senate Committee on Banking and Currency, 86th Cong., 1st Sess. (1959) 18

PAGE

Commentaries

3 A. BROMBERG & L. LOWENFELS, SECURITIES FRAUD & COMMODITIES FRAUD (1981) 16 n.12

Fischel, *Secondary Liability Under Section 10(b) of the Securities Act of 1934*, 69 CAL. L. REV. 80 (1981) 15, 17

Ruder, *Multiple Defendants in Securities Law Fraud Cases: Aiding and Abetting, Conspiracy*, In Pari Delicto, *Indemnification and Contribution*, 120 U. PA. L. REV. 597 (1972) 14

Steinberg and Gruenbaum, *Variations of "Recklessness" After* Hochfelder *and* Aaron, 8 SEC. REG. L. J. 179 (1980) 7 n.5

Wheeler, *Plaintiff's Duty of Due Diligence Under Rule 10b-5: An Implied Defense to an Implied Remedy*, 70 NW. U. L. REV. 561 (1976) 8 n.7

Comment, *A Reevaluation of the Due Diligence Requirement for Plaintiffs in Private Actions Under SEC Rule 10b-5,* 1978 WIS. L. REV. 904 (1978) 8, 8 n.7, 8 n.8

Other

RESTATEMENT OF TORTS § 286 (1934) 15 n.11

RESTATEMENT OF TORTS § 876 (1939) 15, 16 n.12

Nos. 80-1684/1691

IN THE

Supreme Court of the United States

October Term, 1980

PEAT, MARWICK, MITCHELL & CO., *et al.*,

Petitioners,

v.

WACHOVIA BANK AND TRUST CO., N.A., *et al.*,

Respondents.

WHITE & CASE AND MARION JAY EPLEY, III,

Petitioners,

v.

WACHOVIA BANK AND TRUST CO., N.A., *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA

BRIEF OF AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS AS *AMICUS CURIAE* IN SUPPORT OF THE PETITIONS FOR A WRIT OF CERTIORARI

PRELIMINARY STATEMENT

The American Institute of Certified Public Accountants ("Institute") submits this brief as *amicus curiae* pursuant to Rule 36 of the Rules of this Court in support of the petitions of Peat, Marwick, Mitchell & Co., *et al.* ("PMM") in No. 80-1684 and White & Case, *et al.* in No. 1691 for a Writ of Certiorari and urges this Court to review and reverse the

decision of the Court of Appeals for the District of Columbia entered on December 5, 1980.[1]

QUESTIONS PRESENTED

The Institute confines its present participation to urging the Court to grant the Writ to review and decide at least the following issues which are subsumed by certain of the questions presented in the Petitions for Certiorari.[2]

> 1. May a private cause of action for damages be implied under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1976) ("1934 Act") in favor of a purchaser of securities who is unable to satisfy the criteria for asserting the express causes of action provided by Section 18 of that Act?
>
> 2. May a private cause of action for damages be implied under Section 10(b) of the 1934 Act against a person who is alleged to be an aider and abettor of a violation of the Section?

The Institute contends that these issues are each fairly presented upon an adequate record in this case. Each issue is of substantial significance to the interpretation and development of the law in the area and was wrongly decided by the Court of Appeals.

1. This brief is submitted upon consent of the parties pursuant to Rule 36.1 of this Court. The written consent of the Respondents in both cases, subject to a condition which has been fulfilled, is contained in a letter of counsel dated May 11, 1981; the consent of Petitioners in No. 80-1684 is contained in a letter of counsel dated May 11, 1981; and the consent of Petitioners in No. 80-1691 is contained in the letter of counsel dated May 14, 1981. True copies of such written consents are being filed simultaneously with this brief with the Clerk of the Court.

2. The Institute has not formulated and does not express any position with respect to the other issues set out in the questions presented in the Petitions for a Writ of Certiorari or upon other issues fairly included therein.

INTEREST OF THE INSTITUTE AS *AMICUS CURIAE*

The Institute is the only national accounting association whose membership is limited to certified public accountants; it now has approximately 160,000 members. Among its purposes are the promotion and maintenance of high professional standards of practice. Pursuant to those purposes, the Institute develops Generally Accepted Auditing Standards ("GAAS") which form the standard of professional conduct for independent public accountants in the examination and expression of an opinion on financial statements, and the Institute has come to be accepted as authoritative in the promulgation and interpretation of standards and procedures in its field.

The Institute thus has a significant interest in the scope and bases of civil liability for damages sought to be imposed upon independent public accountants who are required to follow GAAS and other Institute pronouncements in connection with their work.

In recognition of this interest, the Institute presented its views on such matters before the United States Senate in 1934 at the time the Senate was considering the scope of civil liability for damages to be provided in the 1934 Act. See *Hearings on S. Res. 84 (72d Cong.), S. Res. 56 and S. Res. 97 (73d Cong.) Before the Senate Committee on Banking and Currency,* 73d Cong., 1st Sess., pt.15, 7207-10 (1934) ("1934 *Hearings*"). This Court has permitted the Institute to file briefs *amicus curiae* on related issues in *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185 (1976); *Touche Ross & Co.* v. *Redington*, 442 U.S. 560 (1979); and *Aaron* v. *SEC,* 446 U.S. 680 (1980).[3]

The decision of the Court of Appeals is representative of a trend in the lower courts to imply causes of action under

3. The Court also granted the Institute leave to file a brief *amicus curiae* in support of the Petition for a Writ of Certiorari in *A. H. Robins Co., Inc. v. Ross,* 446 U.S. 946 (1980) although the Court denied the Writ of Certiorari therein.

Section 10(b) with considerable liberality. Auditors, because of the significance of their role in the dissemination of financial information to investors, are particularly vulnerable to such implied causes of action. The accounting profession and the Institute thus have an important stake, beyond the concerns of the immediate litigants, in the appropriate doctrinal and practical development of the jurisprudence of the 1934 Act. The Institute submits this brief to express its view that the present case raises issues of far-reaching significance that should be decided by this Court.

SUMMARY OF ARGUMENT

The opinion below is typical of lower court decisions which have interpreted the federal securities laws expansively by implying private rights of action. These decisions abound despite this Court's repeated admonitions that such actions should be implied sparingly. The lower courts have undertaken this expansion by *inter alia* answering questions that have been left open by this Court in a manner which is clearly inconsistent with the Court's rulings.

Two examples of such judicial expansion exist in this case. The Court of Appeals held that a private cause of action for damages may be implied under Section 10(b) of the 1934 Act in favor of a purchaser of securities who is unable to satisfy the criteria for asserting the express cause of action provided by Section 18 of that Act. The Court so held even though the language of Section 18 and its legislative history clearly demonstrate that Congress made a conscious decision to define specifically the extent of a private cause of action under Section 18. The holding is also at odds with this Court's recent pronouncements that the existence of an express cause of action in a statutory framework tends to show that an implied cause of action was not intended by Congress.

The Court of Appeals also decided that a private cause of action may be implied against a party who aids and abets a violation of Section 10(b). The implication of this private remedy by the Court below as well as many other lower courts is apparently premised on a tort law analogy that has been explicitly rejected by this Court. Because there is no evidence in the language or legislative history of Section 10(b) that Congress intended to create a private right of action against aiders and abettors under that section, there is absolutely no foundation for the Court below to do so.

This Court should grant the writ in these cases to decide now certain hitherto open questions and to provide urgently needed guidance to the lower courts as to the existence and scope of implied remedies under the 1934 Act. Litigation asserting such remedies continues to proliferate and the decisions rendered by the courts below reflect substantial confusion which this Court should promptly address.

REASONS FOR GRANTING THE WRIT

A.

THE HOLDING BELOW IS REPRESENTATIVE OF A TREND OF LOWER COURT DECISIONS WHICH DISREGARD THE LIMITATIONS ON IMPLIED CAUSES OF ACTION ANNOUNCED BY THIS COURT.

The Court below decided that an implied private cause of action for damages exists under Section 10(b) of the 1934 Act: (a) in favor of purchasers who were unable to obtain the remedies expressly provided in the 1934 Act; and (b) against professionals who were not sellers of securities but who allegedly aided and abetted others in violation of that Act. The Court of Appeals thus answered two of the questions about the scope of implied civil remedies which were explicitly reserved by this Court in *Ernst & Ernst* v.

Hochfelder, supra at 192 n.7, 211 n.31.[4] In each instance, the Institute contends that the Court of Appeals erred for reasons briefly discussed in parts B and C below.

If there were no more to this case than a discrete incident of error in deciding open questions of federal securities law, the Institute might not urge this Court to grant certiorari to review the matter. But there is more to the case.

The decision below is a paradigm of those cases in which lower courts have increasingly seized upon questions left open by this Court to develop expansionist applications of Section 10(b) of the 1934 Act along lines that are quite plainly at odds with the teachings of this Court's recent decisions. Open questions, of course, are open; but the lower courts seem to be deciding these issues inconsistently with the doctrinal pronouncements of this Court in the area. Examples of this propensity to exploit open issues in aid of the aggressive implication of remedies under the 1934 Act abound; a few will suffice to make the present point.

This Court has twice left open the issue of whether recklessness could, in some circumstances, satisfy the requirement of *scienter* under Section 10(b). *Ernst & Ernst* v. *Hochfelder, supra* at 194 n.12; *Aaron* v. *SEC, supra* at 686 n.5. The lower courts have rushed to fill that vacuum, repeatedly finding that recklessness will suffice to support a claim for damages under Section 10(b).[5]

4. The District Court also addressed a third issue left open by this Court—whether there is a cause of action available under Section 17 of the Securities Act of 1933, 15 U.S.C. § 77q (1976) ("1933 Act"). *Wachovia Bank and Trust Co., N.A. v. National Student Marketing Corp.*, 461 F. Supp. 999, 1004-07 (D.D.C. 1978). *See Aaron* v. *SEC*, 446 U.S. 680, 689 (1980); *International Brotherhood of Teamsters* v. *Daniel*, 439 U.S. 551, 557 n.9 (1979); *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 733 n.6 (1975). The Court of Appeals pretermitted the issue, Appendix to PMM Petition at 18a-19a n.19, while noting that the circuits were in conflict on the point.

5. *E.g., Huddleston* v. *Herman & MacLean*, 640 F.2d 534, 544-47 (5th Cir. 1981); *Healey* v. *Catalyst Recovery of Pa., Inc.*, 616 F.2d 641, 649 (3d Cir. 1980); *Mansbach* v. *Prescott, Ball & Turben*, 598 F.2d 1017,

(footnote continued)

While these cases acknowledge *Hochfelder,* they rely heavily on the familiar invocation of the remedial purposes "underlying the federal securities laws" as justifying their liberal construction. *See, e.g., Mansbach* v. *Prescott, Ball & Turben,* 598 F.2d 1017, 1024-25 (6th Cir. 1979), *citing, Affiliated Ute Citizens* v. *United States,* 406 U.S. 128, 151 (1972). These cases do not pay similar deference to the repeated cautions by this Court that remedial gaps in congressional legislative schemes are not to be filled by judicial interpretation,[6] nor to this Court's explicit recognition that the remedial purposes of the 1934 Act do not provide a license for expansive judicial interpretation of its provisions. *Touche Ross & Co.* v. *Redington, supra* at 578; *SEC* v. *Sloan,* 436 U.S. 103, 116 (1978); *Ernst & Ernst* v. *Hochfelder, supra* at 200. This Court has recently reiterated that this constraint springs from the constitutional limitations upon the federal courts as tribunals of limited jurisdiction and from the constitutional imperative that the courts defer to the Congress for the development of remedial legislative schemes. *E.g., Kissinger* v. *Reporters Committee,* 445 U.S. 136, 149-50 (1980); *California* v. *Sierra Club,* —U.S.—, 49 U.S.L.W. 4441, 4444 (April 28, 1981); *Touche Ross* v. *Redington, supra* at 578-79; *Cf. Milwaukee* v. *Illinois,* —U.S.—, 49 U.S.L.W. 4445, 4447 (April 28, 1981).

The result of this generous interpretation of the *scienter* element of Section 10(b) has been the creation, through a

---

(footnote continued)
1023 (6th Cir. 1979); *Nelson* v. *Serwold,* 576 F.2d 1332, 1337 (9th Cir.), *cert. denied,* 439 U.S. 970 (1978); *Rolf* v. *Blyth, Eastman Dillon & Co., Inc.,* 570 F.2d 38, 44 (2d Cir.), *cert. denied,* 439 U.S. 1039 (1978); *Sunstrand Corp.* v. *Sun Chemical Corp.,* 553 F.2d 1033, 1039-40 (7th Cir.), *cert. denied,* 434 U.S. 875 (1977). See, Steinberg and Gruenbaum, *Variations of "Recklessness" After* Hochfelder *and* Aaron, 8 SEC. REG. L. J. 179 (1980).

6. *E.g., California* v. *Sierra Club,* —U.S.—, 49 U.S.L.W. 4441, 4444 (April 28, 1981); *Universities Research Ass'n* v. *Coutu,* —U.S.—, 49 U.S.L.W. 4354, 4358 (April 6, 1981); *Transamerica Mortgage Advisors* v. *Lewis,* 444 U.S. 11, 15-16, 23-24 (1979); *Touche Ross & Co.* v. *Redington,* 442 U.S. 560, 578 (1979). *See also, Cannon* v. *University of Chicago,* 441 U.S. 677, 740-45 (1979) (Powell, J., dissenting).

developing federal common law, of an implied cause of action for behavior well short of "knowing or intentional misconduct." *Compare, Aaron* v. *SEC, supra* at 690; *Ernst & Ernst* v. *Hochfelder, supra* at 197.

These developments in the doctrine of *scienter* have spawned a cognate line of cases having remarkably anomalous consequences. These decisions hold that, whereas before *Hochfelder* a plaintiff could be obligated to prove due diligence in one form or another in order to make out his case,[7] after *Hochfelder,* only recklessness on the part of the plaintiff, demonstrated affirmatively by the defendant, could bar recovery.[8] The logic of these cases appears to be that since his burden of proof as to the defendant's state of mind has been increased, the plaintiff's burden of proof as to his own culpability should be eased. Whatever one may think of this emerging rule as a proposition of logic or of policy, see *Dupuy* v. *Dupuy,* 434 U.S. 911 (1977) (White, J., dissenting from denial of certiorari), its acceptance in the Courts of Appeals has mushroomed since *Hochfelder.* See Comment, *A Reevaluation of the Due Diligence Requirement for Plaintiffs in Private Actions Under SEC Rule 10b-5,* 1978 WIS. L. REV. 904, 911 (1978).

These cases ascribe to *Hochfelder* the remarkable consequence of expanding the implied cause of action available

7. *E.g., Hirsch* v. *du Pont,* 553 F.2d 750, 762-63 (2d Cir. 1977); *Rochez Bros., Inc.* v. *Rhoades,* 491 F.2d 402, 409 (3d Cir. 1974), *cert. denied,* 425 U.S. 993 (1976); *Clement A. Evans & Co.* v. *McAlpine,* 434 F.2d 100, 104 (5th Cir. 1970), *cert. denied,* 402 U.S. 988 (1971); *City Nat'l Bank* v. *Vanderboom,* 422 F.2d 221, 230 (8th Cir.), *cert. denied,* 399 U.S. 905 (1970). See also, Wheeler, *Plaintiff's Duty of Due Diligence Under Rule 10b-5: An Implied Defense to an Implied Remedy,* 70 NW. U. L. REV. 561 (1976); Comment, *A Reevaluation of the Due Diligence Requirement for Plaintiffs in Private Actions Under SEC Rule 10b-5,* 1978 WIS. L. REV. 904 (1978).

8. *E.g., Mallis* v. *Bankers Trust Co.,* 615 F.2d 68, 77-79 (2d Cir. 1980); *Dupuy* v. *Dupuy,* 551 F.2d 1005, 1013-24 (5th Cir.), *cert. denied,* 434 U.S. 911 (1977); *Sunstrand Corp.* v. *Sun Chemical Corp., supra* at 1048-49; *Holdsworth* v. *Strong,* 545 F.2d 687, 692-95 (10th Cir. 1976), *cert. denied,* 430 U.S. 955 (1977); *Straub* v. *Vaisman & Co.,* 540 F.2d 591, 596-98 (3d Cir. 1976). See Comment, *op. cit. supra* 1978 WIS. L. REV. at 911 *et seq.*

under Section 10(b) to previously debarred plaintiffs who were negligent in the protection of their own affairs. This is expansionist common law judgecraft in full flight.

Or, again, consider the implication of a cause of action under Section 17(a) of the 1933 Act, a question which, as we have previously noted, has three times been left open by this Court. See note 4, *supra*. The lower courts virtually uniformly have reached the conclusion that an implied cause of action is available under that section notwithstanding the availability of express causes of action under both the 1933 Act and the 1934 Act. The discussion of the matter by the District Court in this case is not atypical. *Wachovia Bank and Trust Co., N.A.* v. *National Student Marketing Corp., supra* at 1004-07. That Court was following with some fidelity the doctrinal developments in the Courts of Appeals. See, *e.g., Kirshner* v. *United States,* 603 F.2d 234, 241 (2d Cir. 1978), *cert. denied,* 442 U.S. 909 (1979); *Daniel* v. *International Brotherhood of Teamsters,* 561 F.2d 1223, 1245-46 (7th Cir. 1977), *rev'd on other grounds,* 439 U.S. 551 (1979); *Newman* v. *Prior,* 518 F.2d 97, 99 (4th Cir. 1975).

Arguably, much of this derives from the implication of a private cause of action under Section 10(b) of the 1934 Act in the first place. The rationale for the implication of that private cause of action at all has since been thoroughly discredited. *Compare Kardon* v. *National Gypsum Co.,* 69 F. Supp. 512 (E.D. Pa. 1946) *with Touche Ross & Co.* v. *Redington, supra* at 576-78. Quite plainly, if that issue were presented now for the first time, no private cause of action would be implied. *Cf. Cannon* v. *University of Chicago,* 441 U.S. 677, 692-93 n.13 (1979); *Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. 723, 729-30 (1975). Although the vast majority of cases recently brought have been at the instance of purchasers, the acquiescence thus far accorded by this Court to the implication of a private cause of action under Section 10(b) has been limited to actions by sellers, to whom no express remedies are afforded by the 1933 or

1934 Acts. *Affiliated Ute Citizens* v. *United States, supra*; *Superintendent of Insurance* v. *Bankers Life and Casualty Co.*, 404 U.S. 6 (1971). In all other respects, this Court has been at pains to prune the "judicial oak" identified in *Blue Chip Stamps* v. *Manor Drug Stores, supra* at 737.

In doing so, this Court has exhibited its customary restraint in not prematurely reaching issues unnecessary for decision. As this discussion indicates, however, the lower courts have typically regarded such reserved questions as comprising an agenda of issues which they were at liberty to address as common law courts bent on nurturing the growth of the 10(b) implied cause of action. Two such fundamental issues are presented here. The Court should accept this case not only to correct the errors of the Court below in deciding these particular issues (to which we next turn), but also to address again the fundamental extravagance which gave rise to those errors in the first place.

B.

IT WAS ERROR TO IMPLY A CAUSE OF ACTION UNDER SECTION 10(b) IN FAVOR OF PURCHASERS WHO WERE UNABLE TO OBTAIN RELIEF UNDER SECTION 18 OF THE 1934 ACT.

This Court has recognized that the existence of an express cause of action in a statutory regime tends to show that an implied cause of action was not intended by Congress to be available. As the Court put it in *Transamerica Mortgage Advisors* v. *Lewis*, 444 U.S. 11, 19 (1979), "... it is an elemental canon of statutory construction that where a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it." *Accord, Universities Research Ass'n* v. *Coutu*, —U.S.—, 49 U.S.L.W. 4354, 4359 n.24 (April 6, 1981); *Kissinger* v. *Reporters Committee, supra* at 148-49; *National Railroad Passenger Corp.* v. *National Ass'n of Railroad Passengers*, 414 U.S. 453, 458 (1974).

This injunction is particularly apt where the cause of action sought to be implied is broader than the explicit causes of action provided in terms by the Act. *Touche Ross & Co.* v. *Redington, supra* at 574; *Blue Chip Stamps* v. *Manor Drug Stores, supra* at 736.

The Court below reached precisely the anomalous result against which these decisions warn. Congress provided an express remedy to purchasers for misleading statements in Section 18 of the 1934 Act. That section, among other things, deals particularly with the liability of persons such as accountants, who provide professional assistance in connection with filings with the SEC. The language of Section 18 and its legislative history and relationship to other portions of the 1934 Act plainly suggest that Congress made a conscious policy choice in defining the contours of the private cause of action established by Section 18 as it did. It comprehensively described which purchasers might sue, whom they might sue and for what they might sue; it established the outer bounds of timeliness for such an action, provided for certain defenses and positioned the burden of proof on key issues implicated in the cause of action it was creating.

All this is clear enough from an examination of the statutory language which, as this Court has frequently observed, is the starting point of analysis. *E.g., California* v. *Sierra Club, supra* at 4443; *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 472 (1977). Moreover, the legislative history of the 1934 Act demonstrates that Congress meant what it said in limiting liability along the lines prescribed in Section 18. While the legislative history of the Act is silent on the existence or ambit of any implied causes of action, *see Aaron* v. *SEC, supra* at 690; *Touche Ross & Co.* v. *Redington, supra* at 571, that history is not similarly silent on the scope of the express causes of action provided by Section 18. Both the Senate Report and the House Report

affirmed that liability and damages with respect to misleading statements contained in filed documents would lie in favor of "a person who in reliance on the statement and in ignorance of its false or misleading character has purchased the security to which it relates at a price affected by it."[9]

The congressional debates also focused on the unavailability of this remedy to a purchaser who did not rely on the allegedly misleading statements. *See, e.g.*, 78 CONG. REC. 7701, 8040 (1934). Similarly, there was direct focus on the policy implications of the statute of limitations and the nature and amount of damages available under the Act. *See, e.g.*, 1934 *Hearings* at 6565, 7208-09; see also, *Blue Chip Stamps* v. *Manor Drug Stores*, *supra* at 736, 740-41. In short, Congress quite deliberately chose to define with care the private civil remedy that would be available to purchasers of securities under the 1934 Act.

Plaintiffs here did not rely on the allegedly misleading statements and did not timely sue under Section 18. They could not, therefore, recover upon the express remedy provided under Section 18.

The Court below found in this circumstance that the express cause of action under Section 18 of the Act was "not available" and did not "adequately dispose of [the plaintiffs'] claim." Appendix to PMM Petition at 33a, 34a. As a result, the Court thought that it could and should imply a cause of action which would be available to the plaintiffs and which would completely dispose of their claim.[10] This was error.

---

9. S. REP. No. 792, 73d Cong., 2d Sess. 21 (1934); H.R. REP. No. 1383, 73d Cong., 2d Sess. 25 (1934). *See also*, S. REP. No. 792, *supra* at 13.

10. Brushing aside as irrelevant to the present case this Court's repeatedly "expressed concern about implying private rights of action when express remedies have been created by statute", the Court below analyzed the express causes of action available under Section 18 and under Section 11 of the 1933 Act to demonstrate that the "express reme-

(footnote continued)

The remedy of Section 18 was unavailable to these purchasers and did not dispose of their claim precisely because the Congress so designed the Act as to make a remedy unavailable to purchasers such as respondents with a claim such as they had. This is not a judgment which the courts are at liberty to reverse because they believe the congressional policy was unwise; nor is the hiatus in remedies produced by the design of the 1934 Act one which the courts are at liberty to fill. *Universities Research Ass'n* v. *Coutu, supra* at 4358; *Touche Ross & Co.* v. *Redington, supra* at 578, 579.

Because the Court below, for reasons of policy, divined a gap in the statutory scheme which departed from that Court's view of the remedial purposes of the legislation it was construing, it implied a cause of action in favor of purchasers who did not rely on the allegedly misleading financial statements and who slept on their rights beyond the period of limitations governing the express cause of action provided by the 1934 Act. The Court, in thus implying a cause of action broader than the express remedies available under the Act, overreached its authority and erred as a matter of law.

The writ should be granted to review and reverse this determination.

(footnote continued)

dies are meant to treat different problems and to be applied in different situations." Appendix to PMM Petititon at 27a-28a. That analysis, of course, begs the question as to whether the different problems and different situations to which the express remedies apply were meant by Congress to be the only problems and situations to which private causes of action should apply. If certiorari is granted by the Court in this case, the Institute will again seek leave to submit an *amicus* brief which will, among other things, examine this issue in some detail.

C.

PRIVATE CAUSES OF ACTION FOR AIDING AND ABETTING VIOLATIONS OF SECTION 10(b) OF THE 1934 ACT SHOULD NOT BE IMPLIED.

This Court has never decided whether civil liability could be imposed for aiding and abetting violations of Section 10(b). *Ernst & Ernst* v. *Hochfelder*, *supra* at 191-92 n.7. Preliminary research indicates that since the time this question was left open in *Ernst*, the lower courts have been faced with the issue on literally hundreds of occasions. These cases typically involve charges against professionals who have allegedly contributed to a violation by a principal perpetrator while they were engaged in their callings. Approximately one half of these cases have involved accountants.

This Court's recent decisions which recognized the limits governing the implication of private remedies under the federal securities laws in general have likewise repudiated the theoretical basis usually employed for such actions against aiders and abettors. Notwithstanding these decisions, however, the lower courts have continued to imply private causes of action for aiding and abetting violations of Section 10(b) against parties engaged in customary business activities such as preparing financial statements and giving legal or investment advice. See Ruder, *Multiple Defendants in Securities Law Fraud Cases: Aiding and Abetting, Conspiracy*, In Pari Delicto, *Indemnification and Contribution*, 120 U. PA. L. REV. 597, 632 (1972). These cases impose upon such professionals the great burden of investigating the activities of the party who is being assisted and of forcing them to defend vexatious actions which are often brought solely for their settlement value. This is an abuse to which this Court has adverted: "[E]ven a complaint which by objective standards may have very little chance of success at trial has a settlement value to the plaintiff out

of any proportion to its prospect of success at trial...." *Blue Chip Stamps* v. *Manor Drug Stores, supra* at 740.

Implied rights of action against an alleged aider and abettor of a Section 10(b) violation have conventionally been based—as were such rights under the securities laws generally[11]—upon common law tort principles. For example, in *Brennan* v. *Midwestern United Life Insurance Co.,* 259 F. Supp. 673 (N.D. Ind. 1966), the Court, after noting that nothing in Section 10(b) or its legislative history indicated a congressional intent to create a private remedy, relied upon the Restatement of Torts § 876 (1939), and held that there was a private right of action against an aider and abettor of a Section 10(b) violation. *See also, Landy* v. *FDIC,* 486 F.2d 139 (3d Cir. 1973), *cert. denied,* 416 U.S. 960 (1974).

This Court has now rejected this tort law analogy as a predicate of implied remedies under the federal securities laws. In *Touche Ross & Co.* v. *Redington, supra* at 568, the Court specifically held that: "[I]mplication of a private right of action based on tort principles, therefore, is entirely misplaced." See, Fischel, *Secondary Liability Under Section 10(b) of the Securities Act of 1934,* 69 CAL. L. REV. 80 (1981) ("Fischel"). Since the tort law analogy was the only rationale for implying a private cause of action against an aider and abettor under Section 10(b), *see id.* at 84, *citing Brennan, supra,* this Court's rejection of that rationale has left the judicially created private cause of action for aiding and abetting without any theoretical underpinning. The special history which has thus far led this Court to a limited acquiescence in the implication of a private right of action on behalf of sellers against principal wrongdoers, *Superintendent of Insurance* v. *Bankers Life and Casualty Co., supra* at 13 n.9, does not provide a basis for extending the reach of that cause of action on the basis of a

11. See, *e.g., Kardon* v. *National Gypsum Co., supra* relying, in the absence of discernible congressional intent, upon the Restatement of Torts § 286 (1934).

now rejected analysis. Indeed, the restraint that should govern such an exercise owes something to principles of constitutional magnitude and cannot be lightly set aside. See, *Cannon* v. *University of Chicago, supra* at 742-47 (Powell, J., dissenting).

Instead of relying on common law tort principles to determine whether to imply a private right of action, the Court has emphasized that "the focus of the inquiry is on whether Congress intended to create a remedy." *California* v. *Sierra Club, supra* at 4444; *Universities Research Ass'n* v. *Coutu, supra* at 4358; *Transamerica Mortgage Advisors, Inc.* v. *Lewis, supra* at 15-16; *Cannon* v. *University of Chicago, supra* at 688. Notwithstanding the Court's repeated holdings that congressional intent is the touchstone for determining whether to imply private remedies under the federal securities laws, however, the lower courts have adhered to tort concepts in implying such private causes of action for aiding and abetting.[12] See, *e.g., Edwards & Hanly* v. *Wells Fargo Securities Clearance Corp.,* 602 F.2d 478, 483 and n.5 (2d Cir. 1979), *cert. denied,* 444 U.S. 1045 (1980).

This recourse to the discredited approach is necessitated by the fact that the securities laws contain no language rendering an alleged aider and abettor liable for damages

12. Since this Court's decision in *Touche Ross & Co.* v. *Redington, supra,* in which the implication of private rights of action based on tort principles was specifically rejected thereby eliminating the sole basis for aider and abettor liability, the lower courts have dealt with aider and abettor liability under Section 10(b) in over 100 cases, many of which have involved accountants. In *IIT* v. *Cornfeld,* 619 F.2d 909 (2d Cir. 1980), for example, the Second Circuit listed the elements of a private cause of action for aiding and abetting a violation of the securities laws. The third element is "'substantial assistance' by the aider and abettor in the achievement of the primary violation." *Id.* at 922. This element is taken from the Restatement of Torts § 876 (1939). 3 A. BROMBERG & L. LOWENFELS, SECURITIES FRAUD & COMMODITIES FRAUD § 8.5(530) at 208.20-.21 (1981). The Second Circuit's test, including the "substantial assistance" element, which is based on tort principles, has been widely used. *E.g., Rolf* v. *Blyth, Eastman Dillon & Co., Inc., supra; Woodward* v. *Metro Bank of Dallas,* 522 F.2d 84 (5th Cir. 1975); *SEC* v. *Coffey,* 493 F.2d 1304 (6th Cir. 1974), *cert. denied,* 420 U.S. 908 (1975); *Landy* v. *FDIC,* 486 F.2d 139 (3d Cir. 1973), *cert. denied,* 416 U.S. 960 (1974).

under Section 10(b) and that the legislative history is not consistent with an implication of such liability.

A look at the statutory language and structure confirms this. Whereas Section 15 of the 1933 Act and Section 20(a) of the 1934 Act impose secondary liability on controlling persons, there is no provision in Section 10(b) for liability for aiding and abetting. It is clear that when Congress intended to impose secondary liability, "it had little trouble in doing so expressly." *Blue Chip Stamps* v. *Manor Drug Stores, supra* at 734; Fischel, *supra* at 97. The express provision of remedies against specific secondary participants again invokes this Court's frequent admonition "that where a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it." *Transamerica Mortgage Advisors* v. *Lewis, supra* at 19. The existence of secondary liability under Section 15 of the 1933 Act and Section 20(a) of the 1934 Act strongly suggests the limitation of congressional intent on the subject and leads to the conclusion that the courts may not imply a private right of action under Section 10(b) against other persons claimed to be secondarily liable.

The inquiry into congressional intent to create a private cause of action for aiding and abetting a Section 10(b) violation is, of course, a fruitless exercise. It was the silence of the legislative history as to congressional intent that originally led the *Brennan* court, *supra,* to resort to tort principles to imply such an action. There is absolutely no evidence in the legislative history of Section 10(b) that would indicate that Congress intended to hold aiders and abettors civilly liable under the Section.

In subsequent reviews of the 1933 and 1934 Acts, Congress failed to enact proposals pertaining to additional aiding and abetting liability. In 1959, for example, the SEC proposed that an aiding and abetting section be added to both the 1933 and 1934 Acts to establish a statutory basis for the proposition that an aider and abettor may be liable

to administrative sanctions or injunctive relief in proceedings brought by the SEC under those sections not containing an express imputation of such liability. *Hearings on S.1178-S.1182 Before a Subcommittee of the Senate Committee on Banking and Currency,* 86th Cong., 1st Sess. 275-76 (1959). In proposing these amendments, the SEC noted a precise limitation on its recommendation: in seeking to extend the aiding and abetting notion from the criminal law[13] to "civil administrative actions by the SEC", *id.* at 288, the SEC Staff specifically recommended that Congress "[m]ake it clear that no civil liability is intended." *Id.* The episode thus reinforced the plain meaning of the statutory framework: there is no private cause of action against aiders and abettors under Section 10(b).

The lower courts' continued use of implied private causes of action for aiding and abetting violations of Section 10(b) despite this Court's recent pronouncements strictly construing the federal securities laws and despite the Court's rejection of the only rationale underlying such actions, creates a great and inappropriate judicial expansion of such secondary liability. The burden of that expansion falls most heavily on professionals such as lawyers and accountants, as this case and any tally of the lower court decisions reflects. Especially when aggravated by liberal interpretations of *scienter* and lowered burdens of proof as to plaintiffs' due care, this undisciplined elaboration of implied remedies poses for those professionals the hazards of vexatious and unlimited exposure against which this Court has warned. *See Blue Chip Stamps* v. *Manor Drug Stores, supra* at 739. The Court should now explicitly resolve this important open issue.

---

13. 18 U.S.C. § 2 (1976).

CONCLUSION

The Writ of Certiorari in these cases should be granted and the judgments of the Court of Appeals reversed.

Respectfully submitted,

KENNETH J. BIALKIN
LOUIS A. CRACO
HOWARD C. BUSCHMAN III
Attorneys for American Institute of Certified Public Accountants
One Citicorp Center
153 East 53rd Street
New York, New York 10022
(212) 935-8000

Of Counsel

WILLKIE FARR & GALLAGHER
MITCHELL J. AUSLANDER
One Citicorp Center
153 East 53rd Street
New York, New York 10022
(212) 935-8000

1980

1981

8080

8085

Z80